COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF:

COMPLIANCE OF KENTUCKY-AMERICAN WATER COMPANY, AMERICAN WATER WORKS COMPANY, RWE AKTIENGESELLSCHAFT AND THAMES WATER AQUA HOLDINGS GMBH WITH THE PROVISIONS OF THE ORDERS APPROVING THE TRANSFER OF CONTROL OF KENTUCKY-AMERICAN WATER COMPANY TO RWE AKTIENGESELLSCHAFT AND THAMES WATER AQUA HOLDINGS GMBH	)))))))))	**CASE NO. 2002-00277**

NOTICE OF CONDITION 34 REPORTS – ANNUAL REPORTS

Come Thames Water Aqua Holdings GmbH, RWE Aktiengesellschaft, American Water Works Company, Inc., Thames Water Aqua U.S. Holdings, Inc. and Kentucky-American Water Company, and pursuant to Condition 34 of the Commission's Order dated December 20, 2002, in Case No. 2002-00317, herewith give notice of the 2007 Annual Report of RWE AG, which is available at www.rwe.com and attached.

Attached hereto electronically are the Consolidated Cash Flow Statement, Consolidated Balance Sheet and Consolidated Income Statement for RWE AG in euros and dollars. The conversion of these statements to dollars is made pursuant to Condition 27 of the Commission's Order dated December 20, 2002, in Case No. 2002-00317, and the converted statements should not be used for any other purpose.

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Respectfully submitted,

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CERTIFICATION

This is to certify that the electronic version of this pleading is a true and accurate copy of the pleading filed in paper medium; that the Petitioners have notified the Commission and the parties in Case No. 2002-00317 by electronic mail on March 31, 2008 that the electronic version of this pleading has been transmitted to the Commission and that a paper copy has been served by mail upon:

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and that the original and three paper copies have been filed with the Public Service Commission on the 1st day of April, 2008.

BY: Lindsey W. Ingram III

Counsel for Kentucky-American Water Company, Thames Water Aqua Holdings GmbH, Thames Water Aqua US Holdings, Inc., RWE AG and American Water Works Company, Inc.

If not us, who else.

Responsible and secure energy supply—the standard by which we are measured.

> Annual Report 2007

2007 key figures at a glance

- ***RWE exceeds forecasts for all major key figures***
- ***Group operating result up 15 %***
- ***Significant decline in net income due to one-off effects in prior year***
- ***Proposed dividend of € 3.15 per share at upper end of target range***

RWE Group		2007	2006[1]	+/- in %
External revenue	€ million	42,507	42,554	-0.1
Germany	€ million	24,840	26,607	-6.6
Outside Germany	€ million	17,667	15,947	10.8
EBITDA	€ million	7,902	7,172	10.2
Operating result	€ million	6,520	5,681	14.8
Income from continuing operations before tax	€ million	5,233	3,537	48.0
Net income	€ million	2,659	3,847	-30.9
Recurrent net income[2]	€ million	2,977	2,466	20.7
Return on Capital Employed (ROCE)	%	16.4	14.2	15.5
Weighted average cost of capital (WACC) before tax	%	9.0	9.0	–
Value added	€ million	2,957	2,074	42.6
Capital employed	€ million	39,710	40,206	-1.2
Cash flows from operating activities	€ million	6,085	6,783	-10.3
Capital expenditure	€ million	4,227	4,728	-10.6
Property, plant and equipment	€ million	4,065	4,494	-9.5
Financial assets	€ million	162	234	-30.8
Free cash flow[3]	€ million	2,020	2,289	-11.8
Earnings per share	€	4.73	6.84	-30.8
Recurrent net income per share	€	5.29	4.38	20.8
Dividend per share	€	3.15[4]	3.50	-10.0
		12/31/07	12/31/06	
Net financial assets of continuing operations	€ million	2,064	4,720	-56.3
Net debt of the RWE Group[5]	€ million	5,056	6,864	-26.3
Workforce[6]		63,439	61,725	2.8

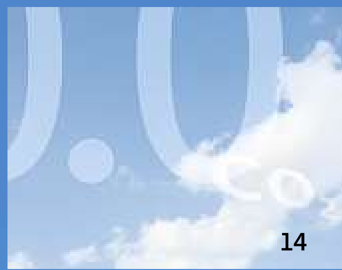
1 Figures partially adjusted; see commentary on page 60.
2 Net income excluding the non-operating result and excluding non-recurrent effects in the financial result, the tax expense and income from discontinued operations.
3 Cash flows from operating activities minus capital expenditure on property, plant and equipment.
4 Dividend proposal for RWE AG's 2007 fiscal year, subject to approval by the April 17, 2008, Annual General Meeting.
5 Net financial assets minus provisions for pensions and similar obligations.
6 Converted to full-time positions; the Water Division is no longer included.

We don’t just talk about protecting the climate—we invest billions.

Contents


6


18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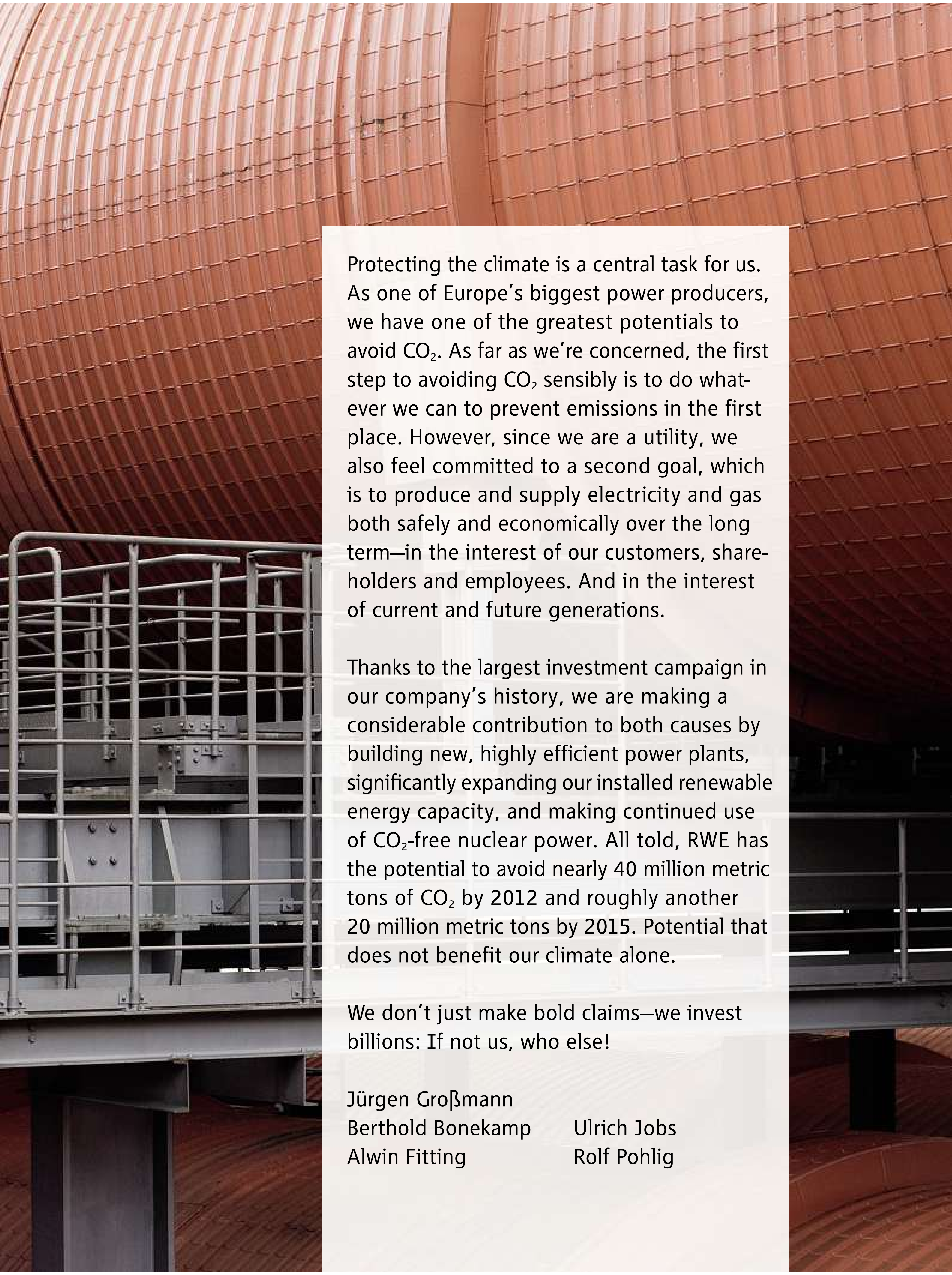
Our mission:
climate protection that pays off



Protecting the climate is a central task for us. As one of Europe's biggest power producers, we have one of the greatest potentials to avoid CO_2. As far as we're concerned, the first step to avoiding CO_2 sensibly is to do whatever we can to prevent emissions in the first place. However, since we are a utility, we also feel committed to a second goal, which is to produce and supply electricity and gas both safely and economically over the long term—in the interest of our customers, shareholders and employees. And in the interest of current and future generations.

Thanks to the largest investment campaign in our company's history, we are making a considerable contribution to both causes by building new, highly efficient power plants, significantly expanding our installed renewable energy capacity, and making continued use of CO_2-free nuclear power. All told, RWE has the potential to avoid nearly 40 million metric tons of CO_2 by 2012 and roughly another 20 million metric tons by 2015. Potential that does not benefit our climate alone.

We don't just make bold claims—we invest billions: If not us, who else!

Jürgen Großmann
Berthold Bonekamp
Alwin Fitting
Ulrich Jobs
Rolf Pohlig


>5

RWE engineers are on a constant quest for new records: They have already used cutting-edge plant technologies to achieve efficiency rates of 43 % in lignite-fired power stations. Furthermore, they are already capable of fine-tuning hard coal power plants to a 46 % efficiency level. Most recently, our engineers have set their sights on obtaining efficiencies in excess of 50 % using novel materials and methods.

Climate protection through energy efficiency

Energy that is not consumed is the most environmentally friendly energy. Therefore, one of our prime objectives is: efficiency! Efficiency in the use of energy throughout our company, in the production of primary energy, in the generation of electricity, and in the consumption of energy by our customers. In our quest to maximize the efficiency with which we use energy, we pursue a holistic approach that runs along our entire value chain: from production and generation to transmission and application. The upshot: CO_2 emissions are reduced, energy costs can fall, and the enhanced productivity improves the security of supply.

Energy source: efficiency! From 1991 to 2006, German companies reduced the amount of energy required per unit of production by some 20 percent. There is hardly a country whose industry makes more efficient use of energy—a boon to the environment, which needs to be built upon. What this means for the energy sector, for instance, is to use less coal to generate the same amount of electricity as before, or employing less electricity and gas without decreasing the quality of life. We are equipped to take on these challenges. In our Rhenish lignite mining region, we are collaborating closely with universities and research institutes developing energy saving belts for our conveyor belt systems, which will reduce power consumption significantly because they run more smoothly. Today, we already save 3.5 million kilowatt hours (kWh) every year by stopping the belts when they are not in use. This corresponds to the amount of electricity consumed by about 1,000 homes in a year. RWE Dea is an icon of economical energy usage on its Mittelplate oil drilling platform in the North Sea: Besides state-of-the-art drilling and production technology, shifting from tanker to pipeline transportation taps substantial savings potential. This eliminates some 1,000 tanker trips a year. And that benefits the environment.

The meter has its own brains: smart metering

More output, fewer emissions. Coal-fired power plants are a pivotal element in the energy supply system. To do justice to climate-protection goals, we have been making progress in various areas since the nineties through our power stations: higher output, fewer emissions and improved efficiency. Our lignite-fired power plants with optimized plant technology (BoA) have set entirely new technological standards: high-tech materials, computer-controlled turbine blades, residual heat recycling and lower in-house power consumption.

Race for efficiency. With an efficiency rate above 43 %, the BoA power plant is roughly twelve percentage points better than the installations that are being replaced by the new BoA 2&3 power stations in Neurath, Germany. While maintaining output, CO_2 emissions will drop by more than 30 percent or—in absolute figures—by 6 million metric tons per year. By building a pilot facility for lignite pre-drying at our power plant in Niederaussem, Germany, we are developing a technique that could enable an efficiency improvement of a further four percentage points. The next engineering goal is

The future F unit of the new lignite-fired power plant, Neurath, Germany: on-site inspection on the boiler frame

the "700 degree coal-fired power plant," which promises to deliver yet another four percentage-point gain. This will put lignite-fired power stations with efficiencies north of 50 % within reach.

Tangible climate relief. Including the BoA 2&3 plants, we plan to invest approximately €8 billion in new power stations on the European Continent through 2012. In addition to a gas-fired power plant in the German Emsland region, we intend to build two hard coal power stations with a thermal efficiency of 46 % and a net installed capacity of over 1,500 MW each. Resulting gains in efficiency will lead to tangible relief for the climate. Compared to older hard coal power plants with a similar capacity, CO_2 emissions will decrease by an annual 2.5 million metric tons per power plant. Two gas power stations planned by RWE npower in the United Kingdom with a combined installed capacity of more than 3,600 MW provide potential savings in excess of 10 million metric tons of CO_2 per annum if—as intended—old hard coal power plants are decommissioned at the same time. All in all, by 2015, our replacement and modernization programme for our UK power stations will decrease specific CO_2 emissions caused by RWE npower by one third compared to the 2000 baseline and by half vis-à-vis 1990 levels.

Energy efficiency at our customers' homes and workplaces. In the spring of 2007, we were the first company in our sector to launch a comprehensive information campaign based on a three-tier pyramid model, in order to increase our customers' awareness of energy efficiency in the private, commercial/industrial and municipal sectors. The second phase encompasses personalized consultation and concrete implementation measures. In this context, we provide our expertise with a view to saving energy and costs together with our customers and being kind to the climate. We provide subsidies primarily targeting street lights and administrative buildings that have poor heat insulation.

Investing in the future! The pyramid's third segment is dedicated to research and development. In order to help our private and commercial customers make more accurate electricity cost calculations, we employ modern computer technology to develop "smart meters," an innovative product that enables one to identify new energy savings potential. Furthermore, our engineers have joined forces with partners to develop the "virtual power plant," which harnesses electricity generated by smaller, distributed block-type thermal power stations and wind power facilities and markets it from a single source. At the same time, the interconnected grid becomes more economical and efficiency is improved. This is one of the reasons for our participation in the "Energy Efficiency" initiative of the German Energy Agency (dena). We will invest €150 million in this programme over three years.

RWE is investigating the possibility of building an innovative wave power plant in the Outer Hebrides' natural environment. The power station's turbines would be driven by airstreams created by the waves. In time, it could supply electricity to 1,500 homes and avoid four metric tons of CO_2 per household per year, which would otherwise result from the use of fossil fuels.


-4 t CO_2

Climate protection through energy from renewables

In the future, energy from renewables—primarily wind and water—will be of central significance in ensuring a sustainable supply of energy. The main reason for this is that renewables do not release greenhouse gases and thus help protect the climate. In the future, renewables' market share will continue to grow. Thanks, in part, to our efforts.

The renewable energy business. We are striving to increase installed renewable energy capacity across Europe. Our objective is to rank among Europe's leading providers of electricity from renewable resources in the next decade. By expanding our renewable energy base, we will make an important contribution to achieving the ambitious goals set by policy-makers in this area at national and European levels. We have thus clearly decided to assign a significant role to renewables-based energy within our strategy. Our commitment is focused on making more use of wind power—both on-shore and offshore. After all, wind will probably be the first renewable resource to pass the profitability hurdle and currently offers attractive growth prospects.

New company: RWE Innogy. We will invest an average of at least €1 billion per annum to increase installed renewable energy capacity. We established RWE Innogy, a new, independent operating management company, effective February 1, 2008. This is the company in which we are pooling our activities and groupwide expertise in the field of renewables. Through RWE Innogy, we have strategically set our sights on the entire European market for renewable energy. RWE Innogy started doing business with an installed power generation capacity of

Baldeneysee, Essen, Germany: RWE run-of-river power plant

North Hoyle off the coast of Wales: RWE offshore wind farm

nearly 1,100 MW, which is more than sufficient to cover demand for electricity in a major city the size of Düsseldorf, Germany.

Wind power. RWE is one of the leading wind power plant operators in the United Kingdom. With North Hoyle, which is located eight kilometres off the Welsh coast, we run the first large-scale offshore wind farm (60 MW) ever built in the UK. This facility generates enough power to cover the amount of electricity consumed by 40,000 homes. Additional growth projects are being planned in the UK, including one of the world's largest offshore wind farms, with an installed capacity of 750 MW. We are also involved in the field of wind power in Spain, France and Poland. Our research and development programme includes the construction of a wave power plant off the Isle of Lewis in the Scottish Hebrides.

Hydropower and biomass. RWE has a long-standing tradition in making use of the force of water. We started expanding a hydroelectric power plant on the upper course of the Rhine last year. In addition, we figure among the largest operators of biomass facilities in Germany. Our biggest biomass-fired power station is located in Berlin and supplies about 20,000 households with electricity. Building on this experience, we will significantly expand our renewable power generation base.

Innovation. Besides expanding installed renewable energy capacity, our new company, RWE Innogy, will become involved in select innovative activities. Technological possibilities are far from being exhausted, especially concerning the use of geothermal as well as wave and tidal energy. We intend to capitalize on this potential profitably. To this end, we will participate not only in conventional research and development projects, but make targeted investments in technology firms and promising new technologies as well.

New storage technique. As electricity from renewables is fed into the grid, there will be significant fluctuations in power supplied. Therefore, it is important to develop efficient electricity storage concepts in good time. We intend to engineer a pressurized air storage power plant in cooperation with General Electric (GE). In periods of high electricity supply, pressurized air storage power plants compress air and store it in underground caverns. This pressurized air can be utilized to generate electricity when needed.

Water, wind and the sun have something in common: They deliver energy, free of CO_2 to boot—just as nuclear power does. Together with other indispensable energy sources, nuclear contributes to a safe, clean, and climate-friendly supply of energy.


CO_2

Climate protection through environmentally-compatible power plants

Nuclear power is a technology that provides energy safely, economically and—above all—free of CO_2. We cannot dismiss the contribution it makes if we want to achieve Germany's and the EU's ambitious CO_2-reduction goals at reasonable cost. We accept political decisions. Nevertheless, we believe that the nuclear phase-out must be reviewed critically. Especially taking issues of climate protection into account. And we want to make coal-based electricity generation environmentally friendly by investing in new technologies. After all, we cannot abandon this energy source in Europe over the short and long term.

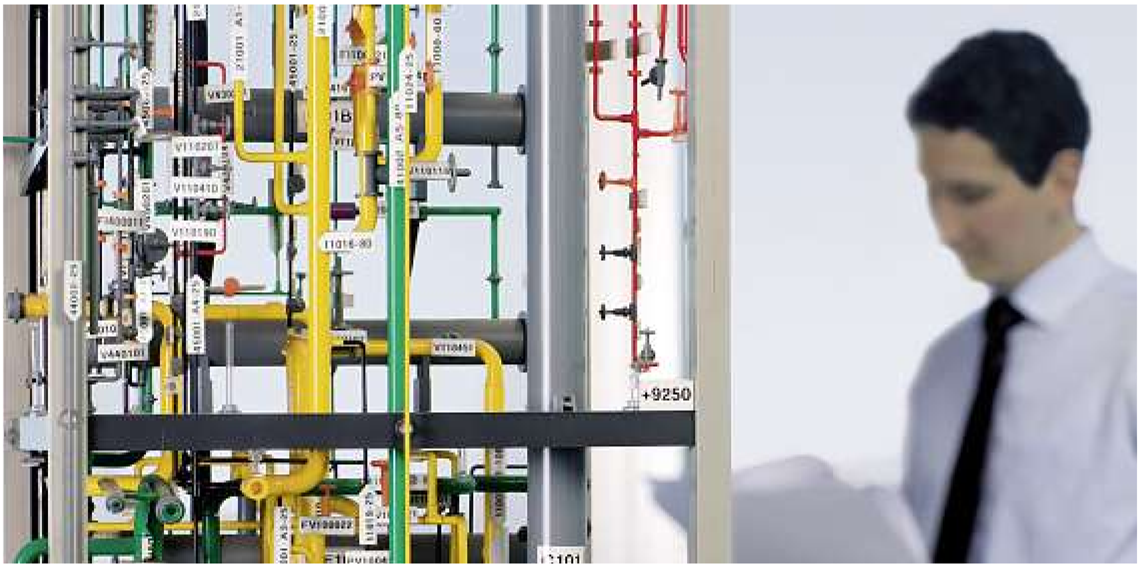
Protecting the climate with nuclear power. About a quarter of the electricity produced in Germany is free of CO_2, thanks to the use of economical and safe nuclear power plants! This spares the atmosphere the burden of bearing some 150 million metric tons of CO_2 every year. Averaged for the EU of 27, nuclear actually accounts for roughly one third of power produced. Otherwise it would hardly be possible to achieve the ambitious climate-protection goals set by the European Union. These targets envision reducing greenhouse gas emissions by at least 20% throughout the EU and by at least 30% in Germany compared with 1990 levels by 2020. In view of this, nuclear power plays a key role in protecting the climate. Germany could follow the examples set by other countries such as the Netherlands, Sweden, the UK and the USA and remain open to a re-evaluation of the nuclear issue and test the phase-out plan depicted by the German Nuclear Energy Act in the context of climate policy.

Biblis nuclear power plant: storage of fresh fuel elements

Balancing ecology and economy. Seeking to gain the time required for such a re-evaluation, we filed a request with the German Federal Environment Ministry to transfer 30 billion kilowatt hours of the power allocation of our decommissioned Mülheim-Kärlich nuclear power plant and of our Emsland nuclear power plant to Unit A of the Biblis power station. The goal is to extend the service life of Unit A until 2012, so that it matches that of Unit B. The continued operation of these two reactor units would spare the environment an annual 15 million metric tons of CO_2. This would not just be a major boon to climate protection—it is also the most macro-economical way to avoid CO_2.

Safety is our top priority. Naturally, safety is always job number one: This is why we have been fundamentally retrofitting the Biblis power plant since 1999, an effort costing €1.2 billion in capital expenditure. An inspection carried out as recently as 2005 confirmed that the facilities meet high safety standards. Today, Unit A satisfies the major requirements defined by the International Atomic Energy Agency (IAEA) for new plants.

Climate-compatible coal power plant from 2014. If we want to ensure a safe and economical supply of electricity, we will not be able to do without coal in the foreseeable future. The alternative that thus remains is to see to it



Clean coal technologies: planning of a coal-fired power station with integrated carbon capture and storage

that coal-based power generation becomes climate-friendly. This goal can only be attained using innovative technologies such as carbon capture and storage (CCS). This technique ensures that CO_2 produced by the power plant is largely captured and then stored under ground—to keep it from escaping into the atmosphere. Our first coal-fired power station with integrated carbon capture and a gross installed capacity of 450 MW is scheduled to be commissioned in 2014. We will invest at least €1 billion in this forward-looking power plant project. At the same time, this key technology will give us the option of producing other products alongside electricity, such as hydrogen and synthetic gas or fuel.

Partner in politics. To implement this large-scale technological project as planned, we need the support of the authorities: Rapid planning and approval processes are a prerequisite for adhering to the ambitious timetable. We need to have a safe legal framework no later than 2009. This applies especially to the transportation and storage of carbon dioxide. In fact, both the EU Commission and the German government have indicated that they are resolutely working towards achieving this goal.

Exporting clean coal technologies. We are concurrently working with partners to develop another technology that adds to CO_2 sequestration, which can also be used in existing power stations: CO_2 washing, which is carried out after combustion. We plan to erect a pilot facility in our lignite-fired power station in Niederaussem, Germany. In the USA, we will join forces with American Electric Power (AEP) to test carbon capture and storage techniques. The objective is to retrofit existing lignite-fired power plants with CO_2 sequestration units by 2020. With the aforementioned technology projects, we will open up new, climate-friendly doors to coal-based electricity generation. Of course, completing development efforts successfully is not enough. We must put these technologies to work in Europe as well. Only then will we be able to offer them as a convincing tool in developing and newly industrializing countries to afford them the opportunity to put their own economic development on sustainable, climate-friendly footing.

Our vision: bridge technologies on the road to the fuel mix of the future. We believe that modern coal-fired power plants can play another important role, serving as a bridge to the fuel mix of the future. What could this mix look like? Renewable energy is the first mainstay of our power generation scenario. Although a lot of development work still lies ahead of us, nuclear fusion has the potential to develop into the second mainstay in the long run. It could develop into the most important pillar of base-load electricity supply. But it faces a long journey. In the meantime, only one source of energy will be capable of meeting the world's growing demand for electricity besides nuclear: coal.

We help developing countries reduce their greenhouse gas levels within the scope of the United Nations' "Clean Development Mechanism." In return, we receive certificates that can be credited to our emissions balance, subject to an annual cap of 18 million metric tons of CO_2 equivalent.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Climate protection through international projects

The Kyoto Protocol obliges industrialized countries to reduce their CO_2 emissions in the period from 2008 to 2012 by at least 5% compared to 1990 levels. As Germany's largest power producer, we are resolutely leveraging our potential to achieve this goal. Our CO_2-avoidance efforts do not stop at the borders of our core markets. We are conducting projects worldwide designed to cut emissions under the auspices of the United Nations, the results of which can be credited to our domestic balance. After all, when it comes to protecting the climate, it does not make a difference whether greenhouse gases are minimized in Europe, Asia, or the Americas.

The industry's room for manoeuvre. With a view to making the planned emissions reduction as economically feasible as possible, in addition to emissions trading, the Kyoto Protocol encompasses two "flexible tools":

First: "Clean Development Mechanism" (CDM). This involves lowering emissions through projects carried out in developing countries. These are financed by RWE, and we receive CO_2 emissions credits from them.

Second: "Joint Implementation" (JI). This involves achieving greenhouse gas reductions working in concert with partners in other industrialized countries. We are taking advantage of both models to obtain emissions allowances and have set aside an investment budget of €150 million for this and other purposes.

In-house and partnership projects. We participate in CDM and JI projects, both through direct investment as well as the acquisition of certificates from third-party projects. Furthermore, we offer plant operators and project engineers our technical know-how with a view to successfully handling and optimally managing suitable projects.

Abu Qir, Egypt: EnviNOx® catalytic converter for the disposal of laughing gas (N_2O) in a fertilizer production facility

CDM and JI projects the world over: RWE's international project team

Emissions allowance purchasing: China as a case in point. China-based Teresa Environmental Industry Co., Ltd., which is active in the fields of recycling, water treatment and biomass processing, has built an "aerobic" composting facility in the Chinese city of Wuzhou in the province of Guangxi. Unlike landfill dumping, aerobic composting avoids the creation of methane. Some 180,000 metric tons in CO_2 equivalent savings could potentially be realized for the period from mid-2007 to 2012. By purchasing associated CO_2 certificates, RWE Power is making a substantial contribution to financing the project costs of €6.5 million, which made the project feasible in the first place. This is the first commercial composting project in the province of Guangxi and is a beacon for other Chinese cities and provinces. The facility has been commissioned and has been registered as a CDM project with the UNFCCC, the relevant UN authority, since July 21, 2007. This gives us the green light to make use of the certificates in Europe.

Proprietary CDM project: India as a case in point. We joined forces with OSRAM, one of the leading companies in the field of lighting technology, to reduce power consumption in select regions in India by employing energy-saving light bulbs. The project will entail distributing to homes compact, energy-efficient fluorescent lamps free of charge or for a nominal fee in exchange for conventional light bulbs. Individual CDM measures will be post-financed by generating emissions allowances. Based on our plans, the first two projects will be cooperative ventures with regional distribution system operators in the states of Haryana and Andhra Pradesh and take place this year. India lends itself to this project because CO_2 emissions specific to the generation of electricity in that country are relatively high. In consequence, reducing power consumption results in a relatively significant decrease in CO_2. Moreover, energy-saving light bulbs are still fairly rare in private households.

Taking stock. By the end of 2007, we had concluded supply agreements for emissions allowances from CDM/JI projects for the period from 2008 to 2010 totalling approximately 24 million metric tons, based on realistic risk assessments. Certificates for first 2 million metric tons have already been allocated to RWE.

Climate protection: conversation with an expert

Coping with climate change represents a momentous technological challenge as well as an economic opportunity for energy companies, says ***Prof. Dr. Klaus Töpfer***. An interview with the renowned environmental expert and former Executive Director of the United Nations Environment Programme (UNEP).

Professor Töpfer, is climate protection to the industry's detriment?
Our planet is currently inhabited by 6.7 billion people. By 2050, the population will have grown to at least 8.5 billion. They all want economic stability, an equitable distribution of welfare, and a secure environment. In turn, demand for energy will increase significantly, and we will no longer be able to cover it solely with fossil fuels. It is not only the development of CO_2 and its effect on climate change that calls for new energy sources and an energy-efficiency revolution—the "hard" goals of energy policy such as competitiveness and security of supply do likewise. This provides major opportunities for an innovative industry that is a technology leader.

Has industry actually understood this?
Most of the industry and consumers have realized that technology and behaviour must be changed in a way that enables us to prosper with less carbon and with substantially fewer natural resources. Industrial managers who have yet to realize this will witness their companies experience significant difficulty in developing. It is those players who have an edge in terms

of energy efficiency, from generation to the household, who are competitive.

What about the power utilities? They certainly don't want to sell fewer products!

Power utilities are increasingly becoming energy service providers. Energy consulting aiming to realize energy savings and investment programmes in the field of energy contracting are emerging as new fields of activity for power utilities. Economic success will not be achieved based on power sales alone, but also on the basis of intelligent efficiency programmes. RWE is capable of assuming a leadership role in this area.

Is the political arena providing the right incentives here?

In spring 2007, the European Union set clear targets with "Agenda 3x20 to 2020:" The German government laid the national foundation for this in the "Meseberg Resolutions."

But will that be enough in the end? After all, climate change is a global problem…

… and climate protection is a global challenge. Our civilization will have to adapt to the realities of global warming. What is also unquestionable, however, is that we must act globally. Even the USA, which is still the world's biggest economic power, is now taking this approach: more energy efficiency, more renewables and clean coal. Modern techniques for energy supply and demand are the markets of the future.

Does this mean that you support technologies for the capture and safe storage of carbon dioxide?

Coal will continue to enjoy worldwide use for a long time, above all in China and India. The challenge lies in massively reducing the impact of coal usage on the climate. Efforts to make carbon capture and storage (CCS) technologies available must be accelerated significantly. German power utilities, including RWE, have established clearly positive positions in this regard. Improved efficiency, alternative energy and clean coal will enable humankind to achieve economic stability and prosperity. This is the decisive challenge. For Germany as well.

And where are we in this regard?

The year 2007 ushered in a pivotal breakthrough as well as a change in investments and consumer behaviour. The report prepared by the World Climate Council, which received the Nobel Peace Prize together with Al Gore, showed that displaying "Three D" behaviour ("Deny, Delay, Do Nothing") is irresponsible. Sir Nicholas Stern has proved that one can limit climate change to a temperature increase of 2 degrees centigrade in an economically feasible manner. The task now at hand is to take advantage of the ensuing opportunities for the benefit of Germany's economy and Germany's consumers as well. RWE's owners, business partners and customers can benefit from the dawn of this new era, too.

Prof. Dr. Klaus Töpfer works and conducts research as a Professor of Sustainable Development at Tongj University in Shanghai.

Major events in 2007

March

Entry into the web-based electricity sales business

RWE acquires sales company eprimo, which sells electricity over the internet. eprimo currently has 200,000 customers.

May

Start of construction of a new gas power plant in Lingen, Germany

Lingen, Germany, will be home to one of the world's most modern combined cycle gas turbine power plants. The power station is to have an installed capacity of 875 MW and is scheduled for commissioning in 2009. It is primarily to be used to cover sudden spikes in demand.

June

New framework conditions for emissions trading

The German Lower House adopts national framework conditions for trading CO_2 emissions allowances between 2008 and 2012. The free allocation of certificates to power utilities is reduced significantly. Some of the allowances are to be auctioned for the first time.

July

Starting shot for the construction of the Rhyl Flats offshore wind farm

The 25 rotors have a combined capacity of 90 megawatts and will be erected in the vicinity of our North Hoyle wind farm, a few kilometres off the coast of Wales. They will supply enough electricity for 100,000 UK households from 2009 onwards.

August

CO_2-reduction strategy

RWE intends to take a series of measures to reduce carbon dioxide emissions and the financial burdens resulting from emissions. The focal points are cutting-edge power plants, the expansion of installed renewable capacity, international climate-protection projects, and the development of new coal-based power generation technologies.

August

Construction of new large-scale power plants given the go-ahead

The construction of two dual-block hard coal power plants of nearly identical design in Hamm, Germany, (1,530 MW) and Eemshaven, Netherlands, (1,560 MW) is planned. Approval processes for both power stations are underway. We want to build another combined-cycle gas turbine power station in the UK, with an installed capacity of about 2,000 MW.

September
German Federal Cartel Office drops case against RWE

The German Federal Cartel Office had conducted an investigation against us for allegedly using improper methods to factor CO_2 prices into electricity tariffs for industrial customers. The basis of the settlement is RWE's agreement to auction limited amounts of electricity generated by its hard coal and lignite power plants.

October
Cornerstone laid for a new gas-fired power plant in the UK

The cutting-edge combined-cycle gas turbine power station will be located in Staythorpe, Nottinghamshire/UK. The plan envisions four units with a total installed capacity of 1,650 MW. The first one is scheduled to go online as early as 2010.

October
Dr. Jürgen Großmann appointed new President and CEO

The 55-year-old owner of Georgsmarienhütte Holding GmbH takes office early, as of October 1. In order to enable a smooth change of leadership, his predecessor, Harry Roels (59), offered an early termination of his contract and resigned from office at the end of September.

October
RWE suggests "Energy Pact for Germany"

This is occasioned by the ongoing conflict between the industry, energy sector and policymakers concerning the development of prices and competition. By proposing an energy pact, we are striving to find solutions to the future's urgent energy matters constructively and—above all—jointly.

November
New renewables strategy announced

We will significantly expand our renewable energy generation base. For this purpose, we will invest at least €1 billion per year. RWE Innogy, our renewables specialist, takes up operations as of February 1, 2008.

November
American Water IPO postponed to 2008

In autumn 2007, we have to postpone our original plan to sell at least a majority of the shares in American Water on the stock exchange before year-end. This was due to the deterioration of the conditions underlying the US capital market.

December
Power plant project in Saarland, Germany, cancelled

We had planned to build a dual-unit hard coal power plant in Ensdorf, Germany. The project failed to get a majority vote in a citizens' poll.

Letter from the CEO

Dear Investor,

My first one hundred days in office as President and CEO of your company are now behind me. This period has gone by very quickly for me. This was not least because my past perspective on the energy sector was largely that of a customer. Another reason is how quickly this industry changes. Energy is and will remain one of the global mega-issues. I cannot recall a time when energy supply matters were such a focal point of public debate since the oil crisis in 1973. Solutions for these issues must be found now. As one of Europe’s largest electricity and gas companies, we will play a prominent role in shaping the future of energy supply. I am proud to be at RWE especially in these challenging times. In my first few months with RWE, I had many conversations with customers and policymakers and I also visited numerous sites. I was impressed by the RWE teams’ know-how and commitment. We do not merely have leading positions in many of Europe’s most important markets—we are among the front-runners when it comes to the reliability and safety of plants and products. However, I also see a lot of room for improvement. We need to do even more to make the customer the centre of our attention. We must be even more creative in examining our business processes to identify ways of improving efficiency. Furthermore, we will take even more determined advantage of our opportunities to grow. And, in the future, RWE has to be a leader in innovation, environmental technology, and the use of renewable energy. In order to achieve all this, RWE does not need to conduct a revolution or actionism. Instead, our company must continue to develop its existing core competencies in the fields of electricity and gas by taking a determined and modern approach—with a more energetic entrepreneurial spirit!

What does worry me is the lack of trust in our entire industry that became apparent recently when I spoke to politicians and customers. Since the liberalization of the energy sector in 1998, substantial progress has been made to create open and fair competition. This brings to my mind Europe’s most liquid wholesale electricity exchange in Leipzig, Germany, the successful work done by the German federal Network Agency, and the rapid increase in household customer switch rates. Nevertheless, the public believes that competition has not really got off the ground and that the price mechanisms are not working. In light of the need for substantial investments in new power plants and grids, such impressions can be fatal, especially when they trigger short-sighted political conclusions, which impede important investment projects. Therefore, the time has come to turn the damaged relationship between the energy industry, policymakers and consumers back into a constructive cooperation. Reactions to our proposed “Energy Pact for Germany” have been encouraging. We have announced new concepts for increased market transparency, more flexible price models and higher energy efficiency. Now, we are putting these ideas into practice.

This rounds up my personal review. What do we intend to do concerning the future of your company? To answer this, I would like to present you with our Strategy Agenda 2012. Its guiding principle is “More Growth, Less CO_2.” Let me start with “growth.” RWE has the potential to remain among Europe’s five largest electricity and gas suppliers in the future. In light of the major wave of consolidation in our sector, you may rightly ask yourself how we intend to achieve this ambitious goal. The most important answer to this question is that we have initiated the biggest investment programme in RWE’s history. We will spend an average of some €6.5 billion in capital on property, plant and equipment per year in the period from 2008 to 2012, increasing our former budget by nearly one-third. Every second euro will be spent on organic growth projects. We also evaluate possible acquisitions. However, we are very selective in this regard, because prices paid to acquire companies are still at a record level.

Our objective is to strengthen and expand the positions we have in Germany and the UK, RWE’s two biggest markets. Centre stage is taken by new power plants with which we want to replace old facilities or gain market share. In this regard, we will focus on large-scale power stations, but also on distributed power generation using combined heat and power technology. We have also earmarked a sizeable budget for electricity and gas grids as well as customer service. New markets are on our list of priorities, too. One of our aims is the gradual entry into growth markets in South-Eastern Europe, including Turkey and Greece. At the same time, we are exploring the possibility of entering into the Russian market. What we also refer to in terms of new markets is the entry into the global liquefied natural gas business and the international gas pipeline business. At the same time, we intend to significantly increase in-house gas production and thus reduce our dependence on gas procurement. Another focal point we have identified is renewable energy. With the newly established RWE Innogy, we want to become one of the leading companies in this field. To this end, we intend to invest an average of at least €1 billion per year. A longer-term goal is to successfully position RWE as a nuclear energy player outside Germany. We are currently in talks over investments in projects in the UK and Central Eastern Europe.

It would be inconceivable for the public debate on the future of energy supply not to address climate protection. European emissions trading will cause power generation costs to rise substantially. We are rising to this challenge by reducing our CO_2 emissions significantly. This is the goal we are pursuing with all our major investment projects in the field of electricity generation. Therefore, we have dedicated this annual report to the issue of climate protection. No power utility in Europe has more potential to avoid carbon dioxide emissions than RWE. We will explain to you how we intend to avoid CO_2 in detail in this annual report. In this context, we also promote making climate protection affordable for customers. Investments in climate-friendly power plant technologies—be it cutting-edge coal and gas units or wind and hydropower—are the most sensible strategies in addition to improving efficiency at the customer’s home or workplace. We question the German government’s planned nuclear phase-out time and again. It would neutralize most of the emissions-avoidance measures that have already been taken and drive up electricity prices.

Improving efficiency is another element of our Strategy Agenda 2012. We will raise our former cost-reduction goal of €600 million by 2010 before year-end. At present, we are conducting a groupwide functional analysis to determine available potential. In so doing, we want to react to the tariff cuts in the regulated German grid business as well as save costs in all areas, while becoming more productive, more competitive, more entrepreneurial, and faster. Another way we intend to enhance efficiency is through the reorganization of tasks at the Executive Board and the combination of RWE Gas Midstream and RWE Trading resulting in the new RWE Supply & Trading. Our goals are to avoid duplication of work, implement decisions more quickly, and pool market competencies.

We are working hard to reflect progress made due to the Strategy Agenda 2012 in value added over the long-term. We have defined new financial targets to enable you to measure us by our results. The benchmark for the period until 2012 is average annual growth of 5% for the operating result and of 5% to 10% for recurrent net income. As you can see, we want your company to display stable growth going forward. This is the best basis for investment and secure jobs as well as for attractive dividends.

I am confident that, with these measures, your company is on course for success. We—the staff as well as my fellow Executive Board members and I—will tackle the challenges facing us in the new fiscal year with all our energy, in order to justify the trust you place in the RWE share. We would appreciate being able to count on your continued support in the future.

Sincerely yours,

Dr. Jürgen Großmann
President and CEO of RWE AG

Essen, February 13, 2008

The RWE Executive Board

Dr. Jürgen Großmann
President and CEO

* March 4, 1952, in Mülheim an der Ruhr, studied ferrous metallurgy and economics, doctorate in ferrous metallurgy, from 1980 to 1993 active within the Klöckner Group, exiting as member of the Executive Board of Klöckner-Werke AG, in 1993 acquired Georgs-marienhütte, from 1993 to 2006 Owner and Managing Director of Georgsmarienhütte Holding GmbH, joined RWE AG as President and CEO effective October 1, 2007.

Alwin Fitting
Executive Vice-President

* March 12, 1953, in Westhofen (Rhine-Hesse), joined the RWE Group in 1974, trained master electrician, from October 2000 to July 2005 Executive Vice-President and Labour Director of RWE Power AG, since August 2005 Executive Vice-President and Labour Director of RWE AG.

Dr. Rolf Pohlig
Executive Vice-President

* December 10, 1952, in Solingen, doctorate in economics, from 2000 to 2006 Executive Vice-President Mergers & Acquisitions at E.ON AG, joined RWE in January 2007 as Executive Vice-President, since May 2007 Chief Financial Officer of RWE AG.

Berthold Bonekamp
Executive Vice-President

* September 2, 1950, in Billerbeck (Coesfeld County), studied mechanical engineering and business management, joined the RWE Group in 1981, since April 2004 Executive Vice-President of RWE AG, from April 2004 to February 2008 concurrently CEO of RWE Energy AG.

Dr. Ulrich Jobs
Executive Vice-President

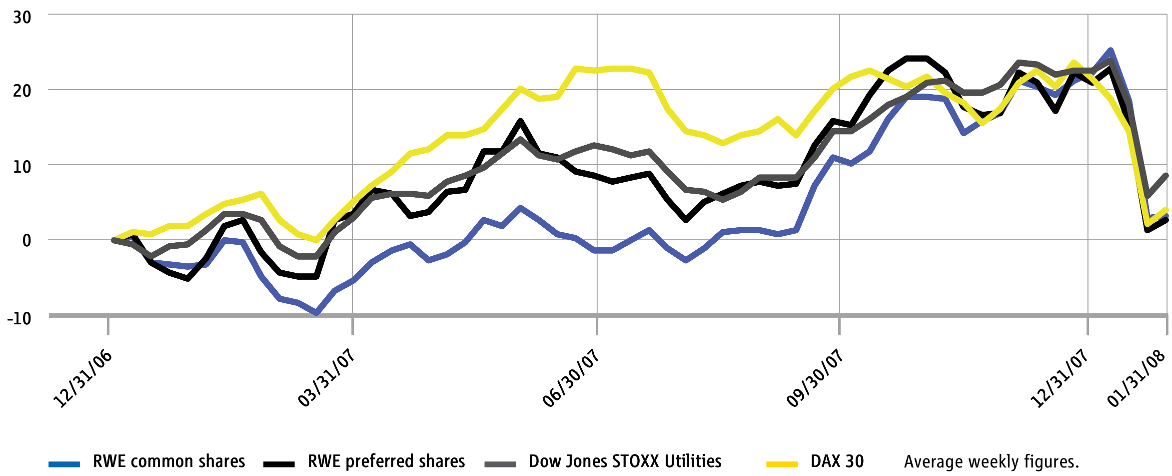
* April 20, 1953, in Herne, holds a diploma in engineering and a doctorate in mining/mine engineering, joined the RWE Group in 1977, since April 2007 Executive Vice-President of RWE AG, from May 2007 to February 2008 concurrently CEO of RWE Power AG.

RWE on the capital market

RWE shares post double-digit growth for the fifth straight year

Our investors enjoyed high returns for 2007: Last year, RWE common shares achieved a total return of 20%. This put us nearly on par with the indices of Germany's blue chips and of European utilities. In contrast, sentiment on the credit markets worsened. The US subprime crisis had a significant impact. This led to higher risk premiums—also for RWE bonds.

Performance of RWE shares compared with the DAX 30 and the Dow Jones STOXX Utilities Indices in %



German share index clearly up thanks to strong first half year. The upward trend on stock markets witnessed since 2003 continued in 2007. Germany's lead index, the DAX 30, closed at the end of the year at 8,067 points. This corresponds to a 22% rise compared to the closing quotation in 2006. A clearly weaker, albeit still positive, performance was recorded by the index of the most important shares in the Eurozone, the Dow Jones EURO STOXX 50. It achieved a total return of 10%. Following a moderate first quarter, stock markets displayed a dynamic upward trend through July. The basis for this was provided by the robust economy, largely positive corporate earnings, and a high level of orders received. Rising crude oil prices and increases in interest rates by central banks did not significantly dampen the positive sentiment on stock markets. On July 16, the DAX closed at 8,105 points, the highest level ever. In the following period, a crisis on the US subprime market overshadowed stock markets. Shares of financial institutions were hardest hit by the loss in investor confidence. Measures taken by the European Central Bank and the US Federal Reserve to support the financial sector, reductions in US interest rates, and the persistently robust economy were instrumental in the initial easing of the situation. However, it became increasingly apparent that the US financial crisis was not over, and fear of recession triggered a sell-off frenzy on stock exchanges at the beginning of 2008. The DAX dropped more than 7% in a single day (January 21). This was the highest single-day loss since the terrorist attacks of September 11, 2001. At the end of January, the index was at 6,852 points.

RWE common share surpasses 100-euro mark for the first time. The development of the value of RWE shares was similarly positive to that of the DAX. At the end of 2007, RWE common shares were listed at €96.00. Last fiscal year, they thus achieved a total return (including the dividend) of 20%. RWE preferred shares closed the reporting year at €83.07, corresponding to a total return of 21%. They thus matched the average for European utilities: The sector index, the Dow Jones STOXX Utilities, also recorded a gain of 21%. The development of RWE's share price in the first half of the year was significantly affected by negative political factors. The framework conditions for CO_2 emissions trading from 2008 onwards were established, among other things. They are resulting in significant added burdens for German utilities. In addition, the government initiative for the tightening of German competition law caused uncertainty. RWE shares gained ground on the overall market and within their sector in the second half of the year. The announcement of the early taking of office of RWE's new President and CEO effective October 1, 2007, was very well received. This news and the development of electricity prices on the wholesale market caused numerous analysts to lift their share price targets for RWE. On January 7, 2008, RWE's common share surpassed the 100-euro mark for the first time (€100.64). However, as stock markets around the world suffered massive declines, RWE shares experienced a substantial loss in value shortly thereafter.

Weighting of RWE shares and RWE bonds in important indices
as of December 31, 2007

Stock index	Weighting in %	Bond index	Weighting in %
DAX 30	5.6	iBoxx Euro Corporates	0.7
Dow Jones EURO STOXX 50	1.9	iBoxx Euro Utilities	7.7
Dow Jones STOXX Utilities	8.9	iBoxx Sterling Utilities	15.0

Comparative performance of RWE shares and important indices up to the end of 2007 in % p.a.	1 year	5 years	10 years
RWE common share	20.0	35.9	10.3
RWE preferred share	21.1	37.2	11.7
DAX 30	22.3	22.8	6.6
Dow Jones EURO STOXX 50	9.6	15.8	7.8
Dow Jones EUROPE STOXX 50	2.6	12.0	5.8
Dow Jones STOXX	2.4	15.5	6.8
Dow Jones STOXX Utilities	21.4	26.8	12.6
REXP[1]	2.5	3.5	4.8

1 Index for the performance of government securities on the German bond market.

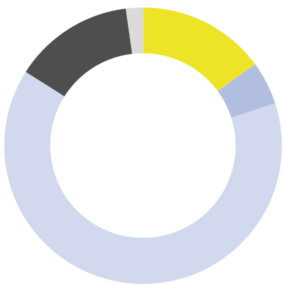
RWE shares delivered much higher long-term returns than the DAX. Long-term investors who invested €10,000 in RWE ten years ago and reinvested their dividends saw their investments grow to €26,566 (common shares) or €30,322 (preferred shares) by December 31, 2007. This corresponds to an annual average return of 10.3% and 11.7%, respectively. The DAX had a total return of 6.6% per annum over the same period of time.

RWE share indicators[1]		2007	2006	2005	2004	2003
Earnings per share[2]	€	4.73	6.84	3.97	3.80	1.69
Cash flows from operating activities per share	€	10.82	12.06	9.43	8.76	9.41
Dividend per share	€	3.15[3]	3.50	1.75	1.50	1.25
Common share price						
End of fiscal year	€	96.00	83.50	62.55	40.70	31.37
High	€	97.90	89.85	63.24	43.50	31.97
Low	€	74.72	61.56	41.10	29.70	17.68
Preferred share price						
End of fiscal year	€	83.07	72.00	54.44	34.21	27.95
High	€	86.00	73.91	55.09	36.94	28.20
Low	€	66.33	54.18	34.79	25.96	16.48
Dividend payment	€ million	1,772[3]	1,968	984	844	703
Number of shares at the end of fiscal year	million	562.4	562.4	562.4	562.4	562.4
Common shares	million	523.4	523.4	523.4	523.4	523.4
Preferred shares	million	39.0	39.0	39.0	39.0	39.0
Market capitalization at the end of fiscal year	€ billion	53.5	46.5	34.9	22.6	17.5

1 In relation to the weighted average number of shares outstanding.
2 Due to a change in IFRS, figures after 2003 no longer include goodwill amortization.
3 Dividend proposal for RWE's 2007 fiscal year, subject to the approval of the April 17, 2008, AGM.

Dividend proposal at upper end of the target ratio. The Supervisory and Executive Boards will propose a dividend of €3.15 per share for fiscal 2007 to the Annual General Meeting on April 17, 2008. Relative to recurrent net income, this results in a payout ratio of 60%. We are thus at the upper end of the target range for the 2007 fiscal year of between 50% and 60%. Based on the closing share prices in 2007, this corresponds to a 3.3% dividend yield on common shares and a 3.8% yield on preferred shares. Therefore, we are among the DAX companies with a strong dividend.

Shareholders structure of RWE AG[1] in %



15 RW Energie-Beteiligungsgesellschaft
5 Capital Research & Management
64 Other institutional shareholders
14 Private shareholders
2 Employee shareholders

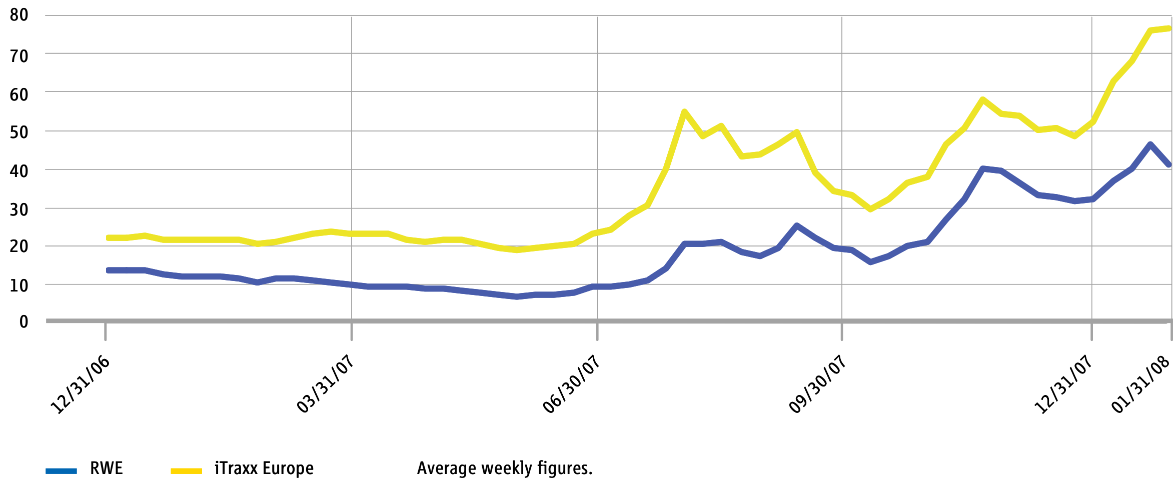
84 Institutional shareholders:
41 Germany
16 US/Canada
13 UK/Ireland
13 Continental Europe excl. Germany
1 Rest of the world

1 Percentages reflect shares in the subscribed capital.
Source: Shareholder identification and notifications of shareholdings in accordance with the German Securities Trading Act (WpHG), as of December 2007.

Shareholder base continues to be broad. At the end of 2007, 84% of RWE shares were held by institutional investors, while 16% were owned by private investors (including employee shareholders). As in the previous year, institutional investors in Germany held 41% of the shares: of these, there is only one notifiable holding, of 15% (2006: 10%), held by RW Energie-Beteiligungsgesellschaft, making it our single-largest investor. Institutional investors in North America and the United Kingdom accounted for a total of 29% of RWE's capital (2006: 30%). Holding roughly 5%, US-based mutual fund Capital Research & Management leads the group of international investors. Institutional investors outside Germany, the UK and North America account for 14% of RWE shares. These investors are domiciled primarily in Continental Europe. The free float serving as a basis for RWE common shares by Deutsche Börse AG in terms of index weighting was 89% at the end of the year.

US subprime crisis unsettles credit investors. Credit markets were affected by the US subprime crisis, especially in the second half of the year. Rising interest rates and declining US real estate prices were the main reasons why borrowers—especially those with low creditworthiness—were no longer able to meet their payment obligations. This caused widespread uncertainty among investors, which intensified at the beginning of 2008. Rising numbers of banks reported losses from their mortgage businesses and related financial instruments. The general fear was that the subprime crisis could jeopardize the economy. As a result, risk premiums on corporate bonds increased. RWE bonds also reflected this development. The price of hedging RWE's credit risk using the five-year credit default swap (CDS) reached a preliminary all-time high of 52 basis points in January 2008. At the beginning of 2007, it was at 15. The European CDS index, iTraxx Europe, which is made up of the CDS prices of 125 major European companies, surpassed the 70 basis-point mark in January 2008.

Development of RWE's five-year credit default swap (CDS) compared with the CDS sector index iTraxx Europe in basis points



Investor relations work: focus on strategy and energy policy. Once again, we maintained intense dialogue with the capital market last financial year. We concentrated on issues of energy policy and—in light of the change in CEO—on the RWE Group's future strategic orientation. We held presentations and Q&A sessions for investors in more than 20 financial centres around the world during more than 50 road shows (on-site visits to investors) and twelve conferences as well as numerous one-on-one meetings. Additional communication activities included presentations published on the internet dealing with sector-related issues such as the European emissions trading scheme and the development of Europe's power generation capacity. We stepped up communications concerning the sustainability of our business activity, since the capital market increasingly assesses companies based on environmental and social responsibility parameters.

Analysts and investors recognize the quality of our communications work. Since 2005, RWE has ranked first in the European utilities category in the two renowned investor relations market surveys conducted by financial information provider Thomson Financial Extel and the trade magazine "Institutional Investor."

Review of Operations

1.0

1.1 Strategy and structure

RWE ranks among Europe's five leading integrated electricity and gas companies. We want to maintain this status. Our market environment is undergoing dynamic change. Competition is becoming fiercer, and the demands placed by our customers on service and product diversity are rising. Furthermore, political and regulatory requirements are becoming increasingly complex. At the same time, Europe's energy markets continue to converge. We have adjusted our strategy in order to take profitable advantage of the resulting opportunities.

More growth, less CO_2: the strategy agenda 2012. We reviewed our strategy in the last few months. We will continue to pursue the main thrusts. But we will establish new points of focus. Continuous earnings growth with fewer CO_2 emissions take centre stage.

- We continue to concentrate our activities on electricity and gas. In so doing, we will expand our renewable energy and gas activities more than before.
- We continue to focus on Europe, while increasing the number of our target markets.
- We intend to occupy leading market positions wherever we have business operations.
- We strive to be successful in all elements of the value chain and supply our customers with electricity and gas from a single source ("integrated business model").
- We aim to continuously increase the value of our company.

Continued focus on electricity and gas. At the end of 2005, RWE made the strategic decision to withdraw from the water sector in the UK and North America. The sale of Thames Water in the UK a year later was the first step. We intend to sell the majority of American Water as quickly as possible, albeit at a reasonable price. We are thus focussing our core competencies on Europe's converging electricity and gas markets. However, water remains part of our business model wherever we already offer our Continental European customers integrated electricity, gas and water services.

Our focus remains on Europe, albeit with a wider geographic scope. Our business currently stretches from the UK to Eastern Europe. This is where we intend to safeguard and further expand our share of the market. We intend to widen our geographic scope within Europe in order to capitalize on additional growth opportunities. We have defined a number of new target markets to this end. In this context, we are assessing privatization opportunities in countries within the EU and bordering the EU such as Russia as well as in South-Eastern Europe, including Turkey. Stable framework conditions are a fundamental prerequisite for investments in this area. One of the objectives behind entering new markets is to give our portfolio a greater regional diversification.

Our strength: leading market positions. Our major power generation, trading and supply markets are currently in Germany, the UK and Central Eastern Europe. In each of these markets, in terms of sales, we rank among the top three suppliers of at least one of our main products, i.e.

electricity or gas. The advantage lies in the fact that leading market positions translate into volume and cost benefits, enabling us to enhance our company's value even when there is significant pressure on prices.

Market positions of the RWE Group	Electricity	Gas
Germany	No. 2	No. 3
UK	No. 3	No. 3
Central Eastern Europe	No. 2 in Hungary No. 3 in Slovakia Starting position in Poland	No. 1 in the Czech Republic Leading position in Hungary
Total Europe	Among the top 5	No. 6

Stability on volatile markets: RWE's integrated business model. Our operations are vertically integrated, i.e. we cover all of the major elements of the value chain. In the electricity business, for example, we are not just producers, but traders, grid operators and a supply company as well. Our vertical alignment affords us greater flexibility in offsetting market fluctuations at the individual stages of the value chain and enables us to make use of synergies. Thanks to our horizontal integration, e.g. the sale of electricity and gas via one regional energy company, we achieve additional synergies. Furthermore, we have bundled our power and gas grids at the distribution network level and placed them in single companies. Since these supply and distribution grid companies have a regional orientation, we can establish and nurture very close ties to our customers.

Active along the entire energy value chain

	Upstream (Generation)			Gas Midstream (Commercial Optimization of Procurement, Transport and Storage) and Energy Trading	Supraregional and Regional Electricity and Gas Grids	Electricity and Gas Supply
	Power Generation	Renewable Energy	Gas and Oil Production			
Continental Europe	RWE Power	RWE Innogy	RWE Dea	RWE Supply & Trading	RWE Energy	
UK	RWE npower					RWE npower

Forward-looking power generation mix. In order to satisfy market demand for electricity, we have a mix of various fuels and technologies. In sum, the RWE Group thus has a well-balanced combination of nuclear energy as well as coal and gas-based power generation. This helps achieve security of supply in times of significant fuel price fluctuations as well as avoid CO_2. In the future, renewables-based energy—especially wind power—will play a much larger role in our mix. This is why we founded RWE Innogy, a company dedicated to this business field. By investing more than €1 billion per year on average, we want to more than triple our portfolio's renewables-based generation capacity by 2012. Furthermore, over the next few years, we will invest in the development of innovative ways to produce electricity from coal in a climate-friendly manner.

CO_2 emissions-reduction strategy. In August of 2007, we presented the cornerstones of a strategy with which we intend to reduce carbon dioxide emissions and the financial burdens resulting from the need to buy CO_2 certificates. We have identified nearly 40 million metric tons in potential reductions by 2012 and slightly more than 60 million metric tons by 2015. These figures are based on the current size of RWE's power plant portfolio. Growth investments have not been factored in. This corresponds to a decline of over 20% by 2012 and more than 30% by 2015, compared to the RWE Group's CO_2 emissions in 2006 (178 million metric tons).

A key element of our strategy is to take part in climate-protection projects within the scope of the Kyoto "Clean Development Mechanism" (CDM) and "Joint Implementation" (JI) mechanism. Companies which participate in the emissions trading scheme can meet their emissions obligations with certificates obtained from these types of projects. However, the EU has set caps for this. Based on our estimates, the allowable amount for our plants in the second trading period (2008 to 2012) is 18 million metric tons of CO_2 per year. The average cost of CDM/JI-sourced certificates is currently far below prices quoted in emissions trading. Further key elements of our CO_2 strategy are the reduction of emissions through the modernization of our power plant portfolio and the expansion of our renewable energy base. We also want to expand the use of combined heat and power generation. In addition, we plan to build the world's first large-scale coal-fired power plant featuring carbon capture and underground storage.

Political decisions in the field of energy policy have a significant impact on the options available to the RWE Group to reduce CO_2 emissions sustainably. The most effective and affordable way to limit emissions is to extend the lifetimes of nuclear power plants. Nuclear power generation emits next to no carbon dioxide, and if the nuclear power stations are shut down, they would have to be replaced by higher-emission fossil fuel-fired power plants. This is because renewables-based power stations are not capable of generating the same amounts of base-load power. We could avoid up to an additional 15 million metric tons of CO_2 emissions per year merely if the lifetimes of our two Biblis units were extended.

Expansion of the gas business. The world gas market is expected to record above-average growth in the next few years. Therefore, we want to expand our activities in this field step by step—at all three stages of the value-added chain. As regards gas production (upstream), we plan to double production by 2012/13—without acquisitions. In the gas procurement, transmission and trading (midstream) business, we intend to strengthen our position in the international transit pipeline sector and establish a position in the liquefied natural gas (LNG) business. With regard to gas sales (downstream), we are primarily exploring entry into new markets, e.g., Central and South-Eastern Europe.

Growing the value of our company sustainably. Increasing the value of our business in the long term in the interest of our investors takes centre stage in RWE's strategy. To achieve this goal, we take the three following approaches:

1. Constant optimization of our existing business: Our "operating excellence" projects are designed to make business processes more efficient and to reduce costs. This year, we intend to raise our current cost-cutting target of €600 million through 2010.

2. Investment in growth: We must make investments today to safeguard our market positions tomorrow. This is the only way for us to continue to achieve stable and attractive returns in the future. Here, the focus lies on our international power plant and grid operations, our oil and gas production activities and—increasingly—on the renewables-based energy business. For this purpose, we have stepped up capital expenditure on property, plant and equipment earmarked for the current and the next four years by nearly one-third to a total of more than €30 billion.

3. Acquisitions that create value: We constantly explore options for expanding our existing portfolio via acquisitions. In so doing, we adhere to our strict strategic and financial acquisition criteria. Acquired activities must at least earn their cost of capital no later than in the third year of their full inclusion. However, given present market conditions, patience is key. Privatization in Eastern Europe is progressing at a moderate pace. Potential for external growth is limited in other regions as well, but bidders are exhibiting keen interest. This results in high purchase prices.

Internal controlling system. Value added is our central controlling instrument. We thus underpin our goal to create value over the long term in the Group's management processes. Value added is calculated by taking each division's return on capital employed, minus the cost of capital. Another means of improving value added besides increasing the operating result is the optimization of asset intensity. The effective management of capital expenditure is key to achieving success in this area. Another lever is the reduction of working capital. We focus on controlling trade accounts receivable and payable and on decreasing inventories.

Value added, in addition to individually agreed goals, is a yardstick for determining the performance-linked compensation of our executives and salaried employees. For details on value management at RWE, please turn to pages 72 et seq. and 208 et seq., respectively.

Change in corporate structure. Our six divisions oversee the RWE Group's operations and manage the business units, which are subordinate to them:

- RWE Power encompasses our Continental European power generation activities (with the exception of energy from renewables), including lignite production.
- RWE Innogy has been in charge of all our renewables activities since February 2008. In its first year, the company will be included in our financial reporting under "Other, consolidation."
- RWE Dea produces oil and gas in and outside Europe. We thus secure a growing share of the Group's gas sales with in-house production.
- RWE Supply & Trading is a new division, in which we will combine RWE Gas Midstream and RWE Trading from 2008 onwards. This division will thus be responsible for the commercial optimization of all our non-regulated midstream gas activities. These consist of the purchase, transmission and storage of gas as well as the LNG business. In addition, as Europe's largest energy trader, the company will be our hub for tradable commodities such as electricity, gas, coal, petroleum, and CO_2 emissions allowances.
- RWE Energy is our supply and grid company for Continental Europe and supplies our customers in this region with electricity, gas and water. Six integrated regional companies operate under this division in Germany, with another six active in our other Continental European markets. Supraregional electricity and gas transmission operations are grouped under legally independent companies, as is our sales business with industrial key accounts.
- RWE npower is responsible for power generation (with the exception of energy from renewables) as well as electricity and gas supply in the UK.

RWE Systems provides internal services for the operating divisions. The company is included in "Other, consolidation" in our financial reporting.

RWE AG is the RWE Group's management holding company, which as such carries out corporate tasks, e.g. Group development, mergers & acquisitions, finance, controlling, executive development and communications.

1.2 Economic and political environment

Economic environment

Economic upturn on RWE core markets continues. The global economy displayed dynamic growth again in 2007. However, the risk to the global economy triggered by the US subprime crisis increased over the course of the year. As a result, the upswing in most industrialized countries lost steam, whereas in newly industrializing countries, it continued nearly unabated.

- According to preliminary figures, in 2007, the Eurozone's gross domestic product (GDP) adjusted to exclude inflation was 2.5% higher year on year. Investing activity against the backdrop of increasing capacity utilization was the economy's driving force. Private consumption was buoyed by positive employment-related effects.

- In real terms, Germany's economy grew by 2.5%, too. Corporate investment in property, plant and equipment was up, driven by the rise in earning power and strong order books. Exports did not rise as much as in the previous year, because the euro rose considerably compared with the US dollar. Consumption displayed weak development despite the improved employment situation. Experts believe this is partially due to the increase in value added tax implemented on January 1, 2007.

- The UK's GDP advanced by 3.1%. As in Germany, one of the reasons for the growth was the rise in corporate investment in property, plant and equipment. Growth in disposable income and the persistently low level of unemployment had a positive effect on consumption.

- The speed of expansion displayed by Central Eastern Europe's EU member states continues to be above average. Rising employment and increasing disposable income drove up consumer spending in these regions as well. There is already a lack of job applicants in certain sectors. Exports and fixed investment contributed to the upturn. According to initial estimates, GDP was up 6% in the Czech Republic, 7% in Slovakia, and 6.5% in Poland. However, growth in Hungary only amounted to 1.5%, as steps taken to restructure the government budget slowed consumption and investing activity.

- In the US, the general economic climate was clouded above all by falling real estate prices and the crisis on the mortgage market. US GDP grew 2.2% over the previous year's figure. Investment in property, plant and equipment and consumption displayed only moderate growth, and construction activity declined. In contrast, the economy benefited from the weak dollar, as it stimulated exports and dampened imports.

However, the aforementioned economic developments only had a limited impact on our organic business trend. Energy consumption generally shows relatively small reactions to changes in GDP.

Economic dynamism is primarily reflected in demand from industrial enterprises. Household energy consumption predominantly depends on the weather.

Demand and price trend

Energy consumption: Mild weather overshadows positive cyclical effects. High temperatures in the first half of the year dampened demand for energy in our core markets. Furthermore, the rise in the level of energy prices caused consumers to reduce usage. A counteracting effect came from the good economic trend displayed by the industrial sector.

Germany's electricity consumption in 2007 was roughly on par with that of the previous year. The weather-driven reduction in demand for electricity for heating purposes was contrasted by expanding industrial output. The decreased need for heating had a much stronger impact on the gas business, causing gas sales to fall by some 5%.

In the UK, electricity usage was down about 3%. As in Germany, the warmer winter reduced the amount of power used for heating purposes. The demand stimulus provided by the industry's economic cycle was unable to offset this. UK gas consumption was up some 3%, despite the weather-induced reduction in demand seen in the household sector. There was a marked rise in gas purchases by UK energy companies. They increased the use of gas-fired power plants in order to benefit from the decline in wholesale gas prices.

The mild weather had an impact on our Central European markets as well. Nevertheless, the economy's strength drove up demand for electricity in Poland and Slovakia slightly, whereas it stagnated in Hungary. Gas consumption was considerably down. In the Czech Republic and Hungary, it was 7% and 11% lower than in 2006, respectively.

Oil prices at record level. Prices on international crude oil markets have risen markedly over the course of the year. The price for a barrel of Brent, which was still at US$50 in January 2007, hit a preliminary record high of US$96 in December. Averaged over the year, a barrel of Brent cost US$72, which was 11% more than in 2006. The main reason for the relative weakness of oil prices early in the year was the unusually mild weather. It dampened oil and gas consumption and led to a rise in crude oil reserves. As the year progressed, however, pressure on demand from newly industrializing Asian countries made itself felt increasingly. This was compounded by price-increasing effects on the supply side: As the conflict between the USA and Iran intensified over the course of the first quarter, market participants feared bottlenecks in the supply of oil from Arab countries. Unrest in Nigeria brought significant parts of the country's oil production to a standstill. Civil unrest in Pakistan was a cause of concern for the markets towards the end of the year. Members of OPEC (Organization of Petroleum Exporting Countries) did not take any effective measures to slow the price increase lastingly.

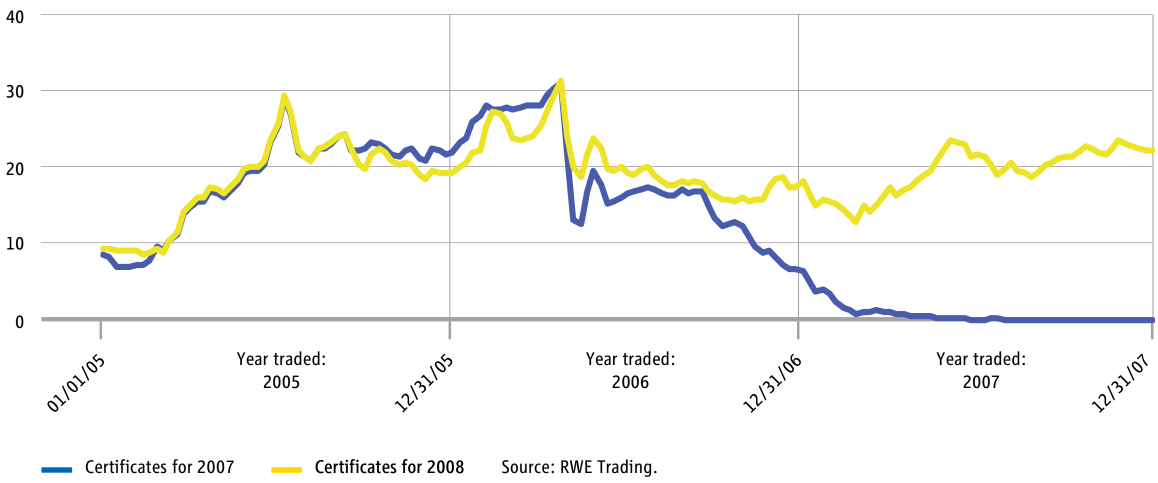
Gas import prices lower year on year. Gas prices on the European Continent are determined to a great extent by developments on the oil market—albeit with a lag of several months. The price of gas imports to Germany declined towards the middle of the year, after which it picked up considerably. It was an average of 7% lower than in 2006. The end customer price trend was steadier. Prices for industrial customers were slightly lower, whereas for households, they were marginally higher. Gas price regulation by the state in the Czech Republic ended on April 1, 2007. Averaged for the year, Czech prices for corporate and industrial customers declined by 9%. In contrast, household gas prices were 2% higher year on year.

Early in the year, UK gas spot prices fell. This was due to the decline in consumption caused by the weather and the commissioning of new import pipelines. They were back on the rise in the second half of the year, in part due to the increase in crude oil prices and the outage of a North Sea pipeline caused by repair work. All in all, industrial enterprises and large corporate customers benefited from the development of gas prices. In contrast, as in Germany, household gas prices were marginally higher compared with the previous year. Contributing factors were the considerable increases over the course of the year in the cost of both gas transmission and of offsetting demand spikes.

Hard coal prices at record level. Analogously to crude oil, hard coal became much more expensive last year. A metric ton of hard coal (including freight and insurance) on the Rotterdam spot market cost US$127 at the end of 2007, as compared to US$67 at the beginning of the year. In the period under review, it thus cost an average of US$89, which was 39% more than in 2006. Coal prices were driven above all by high demand in India and China as well as transport bottlenecks in South Africa and Australia. Furthermore, sea freight rates increased significantly. In 2007, the standard route from South Africa to Rotterdam cost an average of US$32 per metric ton. This is twice as much as in 2006. Prices exceeded US$50 on occasion. This was in part due to the backlog in loading ocean freighters in Australia's coal ports, which led to a reduction in high sea fleet capacity.

German hard coal prices are determined by the German Federal Office of Economics and Export Control (BAFA). They track developments on international coal markets, albeit with a lag of several months. BAFA prices in the first three quarters of 2007 amounted to €65 per metric ton of hard coal equivalent. A figure of €77 is estimated for the fourth quarter. This would put the BAFA price for 2007 far above the prior year's level (€62). If it were not for the US dollar's weakness compared to the euro, it would have risen even more.

Development of CO_2 certificate prices in the European emissions trading system in €/metric ton of CO_2

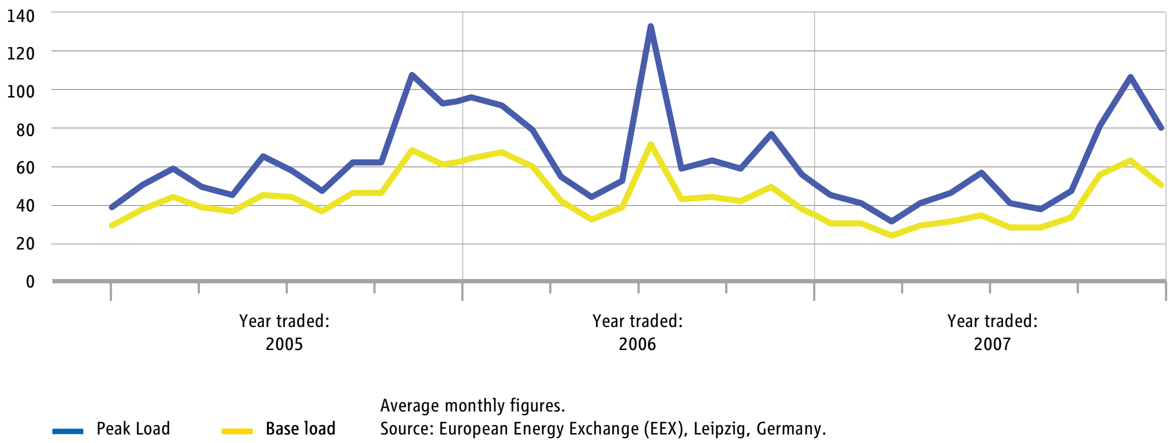


Source: RWE Trading.

CO_2 emissions trading: collapse in prices for 2007 certificates. The dramatic decline in the price of CO_2 allowances for 2007, first witnessed in 2006, continued. The price of a one-metric-ton CO_2 certificate was €6.50 at the beginning of 2007. In February, it fell below the one-euro mark for the first time. It closed the year at a mere 2 euro cents. The expectation prevailing on the market was that companies would have enough certificates in the first trading period (2005 to 2007). This assessment was confirmed by the emissions balances of EU countries for 2005 and 2006. In both these years, aggregate CO_2 emissions by companies participating in the emissions trading scheme were lower than the number of certificates issued. Conversely, certificates are expected to become scarce in the second trading period (2008–2012). This is because the national allocation plans envision reductions in emissions caps—some of which will be considerable—from 2008 onwards. This is reflected in the price of emissions allowances for 2008, which traded at an average of €20 per metric ton of CO_2 in the year under review. The significant difference in price between 2007 and 2008 certificates arises because emissions certificates for the first trading period cannot be carried over to the second trading period.

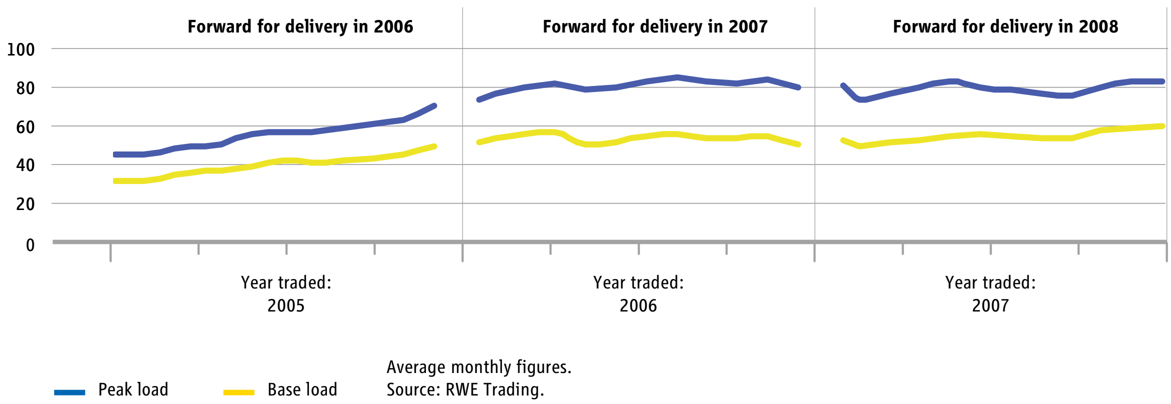
Electricity forward prices remain high. Developments on Europe's electricity wholesale markets were mainly characterized by the high price of fuel. An important contributing factor was the CO_2 certificate price trend in emissions trading. In addition, the forward price trend shows that market participants expect power generation capacity to become tighter over the long term. In spot trading, price-dampening weather effects had an impact.

Development of wholesale electricity spot prices in Germany in €/MWh



Average monthly figures.
Source: European Energy Exchange (EEX), Leipzig, Germany.

Development of one year forward wholesale electricity prices in Germany in €/MWh



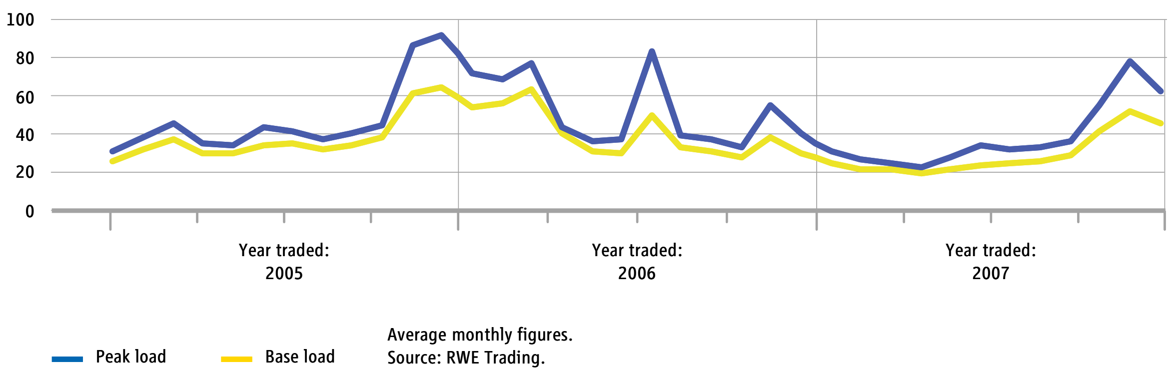
Average monthly figures.
Source: RWE Trading.

In spot trading on the European Energy Exchange (EEX) in Leipzig, Germany, base-load contracts traded at an average of €38 per megawatt hour (MWh), while peak-load contracts sold for an average of €56 per MWh. Compared with the corresponding period in 2006, this represents a decrease of 25% and 23%, respectively. Declining 2007 CO_2 certificate prices were one of the causes. In the first half of the year, the mild weather and the large amount of wind energy generated were the reason for low electricity prices. In the autumn, however, prices picked up considerably. Contributing factors were outages at several German nuclear power plants and a rise in electricity exports to France, where strikes and maintenance work limited power plant availability. In German electricity forward trading, prices were much higher than on the spot market. This is partially due to price differences in CO_2 certificate costs. Forward contracts sold in 2007 for delivery in 2008 cost an average of €56 per MWh (base load) and €79 per MWh (peak load). Corresponding prices for contracts sold in 2006 for delivery in 2007 were €55 and €81 per MWh, respectively.

We sell forward almost all of our in-house production in order to reduce volume and price risks. Therefore, the price developments described above did not have a noteworthy effect on the revenue we generated in 2007. What was decisive was the prices at which forward contracts for delivery in 2007 were concluded in earlier years. We benefited from the fact that prices on the electricity trading market have been on an upward trend since 2002. Our German electricity generation for delivery in 2007 sold for an average of €47 per MWh. By comparison, forwards for delivery in 2006 traded at an average of €38 per MWh. This results in a rise of 24%.

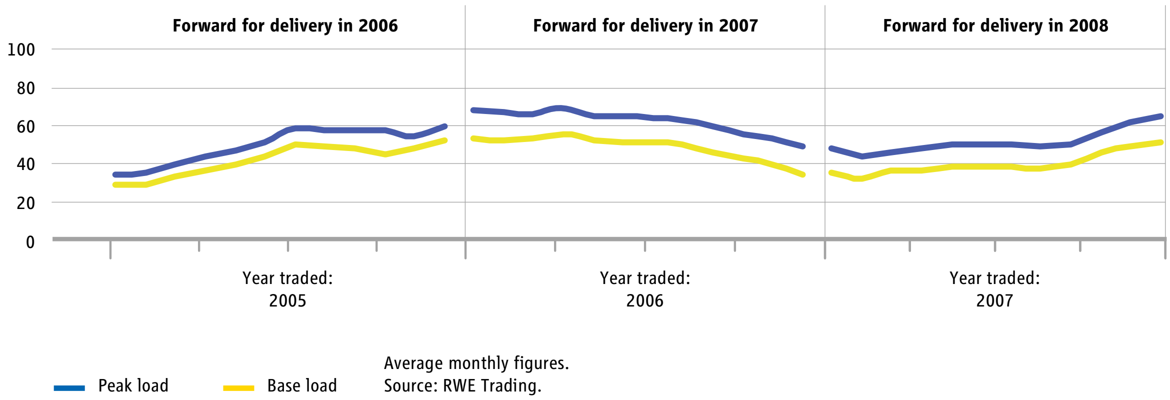
Electricity prices for German end customers displayed disparate developments. Prices for industrial customers fell by an average of 2% year on year due to the development on the wholesale market, especially in spot trading. In contrast, tariffs for households and small commercial enterprises were up between 3% and 4%. The increase in value added tax at the beginning of the year generally caused prices to rise. In addition, burdens resulting from the German Renewable Energy Act (EEG) became more severe. According to the EEG, German grid operators are obliged to pay fixed fees for electricity from renewable sources, most of which are much higher than prices on the electricity market. The law includes a Germany-wide compensation mechanism: Fees paid are allocated to all grid operators, who then pass them through to the end customer via electricity prices. According to estimates by the German Energy and Water Association (BDEW), power produced in compliance with the EEG in 2007 amounted 67 billion kWh. This is one-third more than in 2006. There has been a considerable increase in electricity generated in wind, biomass and solar power plants. The average price for electricity fed into the grid under the EEG was also up. In 2007, it amounted to 11.06 euro cents compared to 10.30 euro cents per kWh in 2006. This reflects the disproportionately strong increase in solar power fed into the grid.

Development of wholesale electricity spot prices in the UK in £/MWh



Average monthly figures.
Source: RWE Trading.

Development of one year forward wholesale electricity prices in the UK in £/MWh



Average monthly figures.
Source: RWE Trading.

Initially, prices on the UK electricity market were significantly down year on year. But they rose in the autumn. Averaged over the year, base-load power traded at £29 (€43) on the spot market. This is 28% less than in 2006. Peak-load power was 25% cheaper, down to £39 (€57). Prices in the UK were still marginally higher than in Germany. The UK market was also marked by the mild weather and the collapse of the price of 2007 emissions certificates. The steep decrease in gas prices was an added factor. Since gas-fired power plants account for a higher share of generation capacity in the UK than in Germany, they have a stronger influence on the formation of electricity prices. Prices on the electricity forward market were also down on the previous year's level, albeit not as much as in spot trading. In the year under review, contracts for delivery in 2008 traded at an average of £41 (€60) per MWh of base-load power, again more expensive than in Germany. This is 17% less than what was paid for a corresponding 2007 contract in 2006. Peak-load forward prices dropped by 16% to £52 (€76).

RWE sells most of the production from its UK power stations forward, in common with the policy it pursues in Germany. Earnings achieved in 2007 thus depended on the price trend in preceding years. Since prices on the forward market had risen considerably by the middle of 2006, RWE npower was able to sell forward its 2007 electricity generation output at prices far exceeding those for 2006 production, as was RWE Power.

Electricity prices paid by industrial enterprises and corporate customers on the UK end customer market declined significantly. Tariffs in these customer segments generally adjust to developments on the wholesale market rapidly due to the form of contracts. They were substantially affected by the decrease in spot prices. End customer prices in the household and small commercial enterprise segments were considerably influenced by the development on the wholesale market as well, albeit with a lag. Therefore, electricity bills for this group of customers went up by an average of 5% to 10%, although power utilities reduced rates during the year.

Electricity prices for end customers in Central Eastern European markets displayed varied developments. Prices for household customers were up more than 13% in Hungary compared with the previous year. In Poland, the price level rose slightly, whereas in Slovakia, it remained stable.

Political environment

The political environment is a key factor for our business. In the year that just ended, the details of the European CO_2 trading system for the period from 2008 to 2012 were decided upon. At the beginning of 2008, the European Commission submitted its drafts for the CO_2 trading period from 2013 to 2020 as well as a draft directive for the promotion of renewables-based energy. At the national level in 2007, the decision to introduce incentive-based regulation in the German grid business effective January 1, 2009, was of special importance to us. The amendment to the German Act Against Restraint of Competition, which entered into force at the end of 2007, may also have a tangible impact on our business.

Allocation act for German emissions trading from 2008 to 2012 passed. On June 22, 2007, Germany’s Lower House established the legal framework for the allocation of emissions allowances in the second CO_2 trading period, which runs from 2008 to 2012. On July 6, 2007, the Upper House gave the go-ahead as well. Germany can distribute allowances for 453 million metric tons of CO_2 to industrial enterprises and utilities every year from 2008 onwards. This is roughly 11% less than in the first trading period (2005–2007) that just ended. Cuts will be made above all in state allocations to power utilities, while the energy-intensive industry, e.g., the chemicals, cement and steel sectors, will continue to receive 98.75% of the certificates they need for free. Power utilities will be faced with additional burdens, since an annual 40 million metric tons of CO_2 of their allotment will be auctioned.

Allowances will be allocated according to a mixed system based on benchmarks and historical emissions. Fuel-dependent emissions standards for natural gas (365 g CO_2/kWh) and coal (750 g CO_2/kWh) in line with the best available technology will be in force. There is no separate benchmark for lignite-fired power plants. A penalty rule will be enforced to further reduce allocations to older—and thus less efficient—power plants. The plants’ average capacity utilization from 2000 to 2005 will be used as a basis for allocating emissions allowances to existing plants. Standard capacity utilization rates will be applied to new plants, i.e., 7,500 hours p.a. for gas and hard coal and 8,250 hours p.a. for lignite.

Plant operators may also meet their emissions targets with certificates acquired through greenhouse gas reduction projects within the scope of the Kyoto mechanisms "Clean Development Mechanism" (CDM) and "Joint Implementation" (JI). The German government has limited the use of JI- and CDM-sourced certificates to 22% of a plant's allocation.

At present, we believe that free certificate allocations between 2008 and 2012 will cover about 60% of our carbon dioxide emissions in Germany. Based on an expected 140 million metric tons in average CO_2 emissions, this corresponds to an allocation covering some 85 million metric tons. In the UK—our second core market—we estimate that emissions from our current power plant portfolio in the same period should average 20 million metric tons per year. We anticipate that we will receive free certificates for approximately 14 million metric tons, or 70%.

European Commission proposes climate protection package for 2013 to 2020. On January 23, 2008, the European Commission presented a new climate protection package for the period from 2013 to 2020. It includes binding goals concerning the reduction of greenhouse gas emissions and the share of renewables in energy consumption for all EU member states. Compared to 1990, the baseline year, these emissions are to be reduced by 20% by 2020. In the same period, the share of renewables-based energy in final energy consumption is to rise to 20%. The EU Commission intends to subject the continuation of CDM/JI projects to the condition that countries in which these projects are carried out ratify an international climate convention for the period starting after 2012.

At an average of 1.85 billion metric tons of CO_2 per annum, the aggregate allocation for the period from 2013 to 2020 is very small. Combined with the restrictive position on CDM/JI projects, this is likely to lead to high CO_2 prices, which will cause electricity prices to rise further. In addition, this would place an especially heavy burden on the energy industry from 2013 onwards, since all of the emissions certificates it requires are supposed to be auctioned. In contrast, other industries only have to bid for 20% of the certificates they need. This share is to rise to 100% by 2020. Energy-intensive companies which are especially exposed to global competition and are at risk of shifting their operations to other countries are an exception in the draft directive. They could continue receiving a free allocation of the certificates they require. However, the Commission does not intend to establish a firm definition of the sectors before 2010.

From our perspective, the approach taken by the EU Commission calls the economic feasibility of the future construction of new, highly efficient coal-fired power plants into question and jeopardizes the status of coal as an important component in the German energy mix.

EU draft directive for the unbundling of electricity and gas grids. Last year, the EU Commission presented a comprehensive energy package, including the corresponding draft directives. This package aims to step up competition on the European energy market and increase security of supply. Another objective is to strengthen the competencies of the national regulatory authorities. Furthermore, the EU Commission wants to establish the foundation for a European regulatory body by introducing an agenda for cooperation among the national regulators.

The directive's package centres on electricity and gas grids. The EU Commission expressed a "clear preference" for a complete unbundling of grid ownership from the rest of an integrated utility's business fields. The Commission claims that ownership unbundling has a positive effect on the intensity of competition and investment in the grid sector. But this allegation has not been proven empirically and is questionable from a scientific point of view. An alternative included in the draft directive is the option of establishing an independent system operator (ISO) for the transmission networks. This would involve transferring all of the transmission grid's business to an independent third party that is not associated with a generation company. The power producer would retain ownership of the grid. Alternatives to ownership unbundling and the ISO are being discussed within the scope of the current political debate on the energy package.

A group of eight member states—including Germany and France—has presented a third model, which aims to ensure free grid access and sufficient investment in the grid infrastructure. In our opinion, drastic changes in ownership rights will not lead to increased competition or be an incentive for investment.

The directive's package will be debated by going through a joint decision-making process in the EU Council of Ministers and the European Parliament. Since European parliamentary elections will be held in June 2009 and the Commission will be re-staffed after that, the package is expected to be adopted by February 2009 at the latest.

Amendment to the German Act Against Restraint of Competition. On December 22, 2007, an amendment to the German Act Against Restraint of Competition (GWB) came into force. It aims to make the monitoring of abuse in the energy sector more effective. Among other things, the amendment envisions stricter monitoring by the state of the way utilities price power. Furthermore, it is now up to the energy utilities to prove the appropriateness of their prices. The burden of proof used to be on the Cartel Office. In addition, antitrust abuse ordinances are now immediately executable, i.e., before cases are settled in court. However, the German Federal Cartel Office will intervene only if there is a substantial difference between the prices charged by the company being investigated and those charged by the companies it is compared to. We are firmly opposed to the amendment. It goes against the EU's requirement to allow prices in the European energy sector to be determined according to the principles of the free market. However, it is currently impossible to estimate the actual impact the change in the law will have. This will depend on the manner in which the Cartel Office and the courts make use of these new tools.

German Upper House adopts incentive-based regulation ordinance for the German grid business. The German Upper House passed the incentive-based regulation ordinance for German electricity and gas grids at the end of September 2007. Following the German government's approval, the ordinance was published in the German Federal Gazette at the beginning of November. Incentive-based regulation is scheduled to be introduced in Germany on January 1, 2009. From this point onwards, grid fees will no longer be calculated on the basis of individual costs alone. Instead, the cost base of grid operators classified as "efficient" by the German Federal Network Agency (efficiency = 100%) will also be taken into account. The first component of the ordinance obliges companies not classified as "efficient" to match the efficiency of the companies to which they are compared within two five-year regulatory periods. No company shall be given an efficiency rating of less than 60%. The ordinance's second component requires all companies to improve their efficiency levels. Efficiency improvements must exceed general productivity gains by 1.25% p.a. for the first regulatory period and by 1.5% p.a. for the second regulatory period. We believe the required efficiency improvements are extremely demanding. Another reason for concern is that the ordinance contains extensive relief for small grid operators, which will cause grid operators to be treated inequitably.

Agreement reached with German Federal Cartel Office on CO_2 costs. The German Federal Cartel Office has dropped its case against RWE, which sought to clarify whether RWE used improper methods to factor the opportunity cost of CO_2 into electricity prices for industrial customers in fiscal 2005. In return, RWE auctions power products from depreciated hard coal and lignite power plants to industrial customers. We remain convinced that taking account of CO_2 costs when determining electricity prices is legally justified. However, we prefer the agreement we have reached with the Federal Cartel Office over protracted litigation. We committed ourselves to offering industrial enterprises a total of 1,575 MW in annual power plant capacity for delivery from 2009 to 2012 in quarterly auctions. This corresponds to a total volume of approximately 46 billion kWh. The starting price will be the full cost of a written-down hard coal or lignite power station. Cost advantages resulting from the free allocation of CO_2 certificates for production from these power plants will be included in the starting price. The first auction was held on February 13, 2008.

German corporate tax reform. In the middle of 2007, the German Lower and Upper Houses passed the German 2008 Corporate Tax Reform Act. The law includes considerable changes that affect the calculation of income and earnings as well as income tax rates. In 2008, the average combined tax on profits for RWE Group companies that are taxed in Germany will drop from about 39% at present to roughly 31%. The necessary reassessment of deferred taxes carried on the balance sheet resulted in a one-off cost of €256 million in fiscal 2007.

"Energy Pact for Germany." At the end of last year, RWE AG's CEO called on policymakers and the public to enter into an "Energy Pact for Germany," in order to address the ongoing confrontation between industry, the energy companies and policymakers over electricity prices and competition on the electricity and gas markets. By launching this initiative, RWE is committing itself to acting constructively—and jointly—to find solutions for the urgent tasks that the energy industry will be facing in the future. We have submitted proposals to this end. The focal topics are new products for energy-intensive customers and households, the increased expansion of renewables-based electricity generation capacity and combined heat and power generation as well as a significant intensification of energy research activities. RWE wants to make a considerable contribution to this cause in all of these areas. Talks with the German Economics Minister, consumer associations and representatives of energy-intensive industries have already commenced.

1.3 Major events

For RWE, 2007 was a year centred on organic growth. We started to build two new state-of-the-art gas-fired power plants as part of the investment programme we initiated to modernize and expand our generation portfolio. Furthermore, we launched a new investment campaign in the field of renewables-based energy. These steps will make our power plants more efficient and climate-friendly. We also made progress in strengthening our position in the European gas business. Conversely, we were unable to complete our focus on energy, our core business, in 2007: We had to postpone the initial public offering of shares in American Water in light of the unfavourable conditions on the US capital market.

Construction of two gas-fired power plants started. In June of 2007, we began to build a combined-cycle gas turbine (CCGT) power station in Lingen, Germany. The investment budget amounts to about €500 million. The power plant, which will have a total net installed capacity of 875 MW, is scheduled for commissioning in 2009. We are constructing another CCGT plant in Staythorpe, UK (Nottinghamshire). We laid the cornerstone for this in October 2007. The power station will encompass four units with a combined installed capacity of 1,650 MW. Some €900 million in capital have been set aside for this project. The first power plant unit is scheduled to go online in 2010.

Additional power stations are still going through the approval phase. One of these projects is the planned construction of a CCGT plant with an aggregate installed capacity of 2,000 MW in Pembroke (UK). Moreover, we plan to build new dual-unit hard coal power stations in Hamm (Germany) and Eemshaven (Netherlands), with an installed capacity of 1,530 MW and 1,560 MW, respectively. We provided commentary on these projects in our 2006 annual report.

Another dual-block hard coal-fired power station with an installed capacity of 1,530 MW was envisioned for the site in Ensdorf, Germany. We cancelled this project due to a lack of public acceptance. The community zoning plan would have had to be changed to accommodate the new power plant. A local referendum on the issue did not result in the majority vote needed to support the re-zoning.

Massive expansion of renewables-based generation capacity. At the end of 2007, we decided to establish a new company in which we would pool our renewable energy activities. The new company took up operations on February 1, 2008. Its registered name is “RWE Innogy” and it is directly assigned to RWE AG. RWE Innogy is in charge of the majority of our existing renewables-based generation capacity and envisions spending an average of at least €1 billion p.a. on new plants from 2008 onwards. We want to more than triple renewable generation capacity by 2012. Wind power projects are the main point of focus. The Chairman of the Board of Directors is Prof. Dr. Fritz Vahrenholt (58), who gained substantial renown through his past entrepreneurial activity and work in the field of energy policy.

1.3 Major events

Today, RWE already ranks among the UK's largest wind power plant operators. We also focus on hydroelectric and biomass projects throughout Europe. In North Hoyle, off the coast of Wales, we already operate a large-scale offshore wind farm, which has a total installed capacity of 60 MW. In July of 2007, we commenced construction on our second offshore wind farm, Rhyl Flats, which is in the immediate vicinity of the North Hoyle wind farm. The facility will have an installed capacity of 90 MW and is scheduled to be commissioned in mid-2009. The investment budget is an estimated €280 million. In addition, we are undertaking preparatory work for the Gwynt y Môr offshore wind farm, which is also close to the Welsh coast. Approximately €2 billion will probably be set aside for this installation. The project is pending approval for construction. With an installed capacity of 750 MW, Gwynt y Môr would be one of the world's biggest offshore wind farms. The first turbines could go online in 2012.

Expansion of position on European gas market. We will significantly expand our gas activities as well. One of our points of focus is the liquefied natural gas (LNG) business. In July 2007, we announced that we wanted to build an import facility for LNG tankers on the German North Sea coast. Our project partner is US-based Excelerate Energy. It uses a technology that enables LNG regasification on board its ships and direct supply of gas into the pipeline network. This reduces investment in infrastructure on land considerably. If the project progresses as planned, we could feed up to 600,000 m^3 per hour of regasified LNG into the German grid from 2010 onwards. A similar Excelerate import facility has been in operation in Teesside in the UK since February 2007.

American Water IPO postponed. In autumn 2007, we had to change our original plan to place at least a majority of the US-based water utility on the New York Stock Exchange by the end of 2007. The main reason for this was that the conditions on the US capital market had deteriorated significantly over the course of the year. If we had conducted the IPO at the end of 2007, we would probably not have been able to achieve a fair value for the company. Our current plan is to carry out the IPO as quickly as possible, while ensuring that we obtain a reasonable price.

Dutch gas grid companies sold. In June 2007, RWE Energy sold its Dutch gas grid companies Obragas Net and Netbeheer Haarlemmermeer to the City of Eindhoven. The transaction value is some €400 million. The sale of these grid activities reduces our annual revenue by about €50 million. In the Netherlands, we will focus on strengthening our sales operations and on power generation, since Dutch regulation prohibits us from expanding our grid activities.

RWE divests investment in RAG. RWE, E.ON and ThyssenKrupp held a combined 90% of RAG Aktiengesellschaft's share capital until November 30, 2007. On this day, their shareholdings were transferred to the RAG Foundation for a symbolic price of €1 each. The shareholders enlisted the services of the accounting firm Ernst & Young to obtain a detailed appraisal of the value of their RAG investment. The appraisal revealed that the shareholdings did not have a positive value. By transferring their stakes, the three RAG shareholders supported an exit from Germany's subsidized hard coal mining sector agreed between the German government and the states of North Rhine-Westphalia and Saarland.

German Federal Cartel Office prohibits acquisition of stake in Saar Ferngas. The German Federal Cartel Office rejected our acquisition of a majority stake in Saar Ferngas AG in March 2007. We filed an appeal with the Düsseldorf Higher Regional Court against this ruling. In May 2006, we had agreed with RAG Aktiengesellschaft to acquire its 77% interest in the southwest German gas utility. At the beginning of July 2007, RAG withdrew from the sales agreement with RWE due to the decision handed down by the Cartel Office. The stake in Saar Ferngas has since been sold to Luxemburg-based ArcelorMittal. Nevertheless, we uphold our appeal before the Düsseldorf Higher Regional Court. The procedure is of fundamental importance to the Group's investment strategy and we want to maintain our right to legal recourse.

Germany-wide electricity sales via the internet. RWE acquired the sales company eprimo after receiving the go-ahead for the transaction from the German Federal Cartel Office in March 2007. The company markets its products through an innovative web-based business model and currently has a base of 200,000 residential and business customers. In October of 2007, we also started marketing gas via the internet through eprimo. We expect to have Germany-wide penetration by autumn 2008. eprimo is designed to complement the traditional offerings of RWE's regional companies, which distinguish themselves by being close to their local customers and providing personal advice.

RWE and Swiss-based EOS exchange hydroelectric and hard coal-based power. In August, RWE Trading and Swiss-based EOS (Energie Ouest Suisse) signed an agreement to exchange power. EOS will obtain electricity from RWE Power's hard coal-fired power plants, mostly on the basis of options, and will cover the cost of associated fuel and CO_2 certificates. In return, RWE received the right to obtain peak-load electricity from EOS hydroelectric power stations. The contract comes into effect on January 1, 2009, and has an initial lifespan of ten years. RWE will probably supply around 1 billion kWh of electricity per year. The agreement to exchange tranches of power is a model for the future: It gives us flexible access to peak-load electricity at short notice, which we would otherwise have to procure on the exchange. Furthermore, this reduces our exposure to CO_2 price risks. The swap agreement with EOS is intended to be a springboard for further transactions of this nature, which we intend to leverage in order to optimize our generation portfolio.

1.3 Major events

RWE funds major portion of pension obligations externally. Effective March 30, 2007, we started funding some of our pension obligations externally. €7.9 billion were transferred to RWE Pensionstreuhand e.V. via a contractual trust arrangement (CTA) and offset against the corresponding provisions for pensions. The funds are earmarked for the financing of pension commitments and may not be used for any other purpose. Our net debt will be unaffected by this transaction, since it includes pension provisions. RWE Pensionsfonds AG was established later in the year. We transferred €4.6 billion in funds from the CTA to the Pensionsfonds. These funds are to cover the pension obligations we have to those of our employees who have already retired.

Gas transmission grid access further simplified. In July of 2007, RWE Transportnetz Gas and E.ON Gastransport agreed to combine parts of their gas grids. They intend to form a common market region for low-calorific gas (L-gas) as of October 1, 2008. By uniting the market regions, they intend to simplify grid access and gas trading, while stepping up competition. RWE Transportnetz Gas had combined its two market regions for high-calorific gas (H-gas) as early as April 1, 2007.

Dr. Jürgen Großmann is RWE AG's new President and CEO. The Supervisory Board of RWE AG appointed Dr. Jürgen Großmann (55) Chairman of the Executive Board of RWE AG effective October 1, 2007. RWE's former CEO, Harry Roels (59), offered an early termination of his appointment ending on January 31, 2008, in order to enable a smooth change of leadership and resigned from office effective at the end of the day on September 30, 2007. Dr. Jürgen Großmann was initially scheduled to join the Group's Executive Board as of November 1, 2007, and assume chairmanship effective February 1, 2008. Jürgen Großmann has been the owner of Georgsmarienhütte Holding GmbH since 1993. He managed that company's business until 2006. Prior to the takeover of Georgsmarienhütte, he held several positions, including one as member of the Board of Management of Klöckner-Werke AG.

Major events after the period under review:

Entry into the Turkish market. At the end of January 2008, we signed a memorandum of understanding in preparation for our entry into the Turkish market. We intend to acquire a stake in a Turkish-based electricity generation company and build power plants with it. RWE has been present in Turkey via an RWE-owned local company since the beginning of 2008. The Turkish economy offers attractive opportunities for growth, since the country's demand for electricity and gas is expected to increase by more than 5% per year. The Turkish government wants to privatize significant parts of the largely state-owned energy supply and electricity generation sectors in the next few years. We are exploring further cooperative and investment projects arising from the privatization process. The country's huge potential in the field of renewable energy is particularly noteworthy.

Nabucco pipeline consortium nominates RWE its sixth partner. Nabucco Gas Pipeline International Ltd., the international consortium for the planning and implementation of one of Europe's most important infrastructure projects for securing gas supplies, announced in early February 2008 the entry of RWE Gas Midstream as sixth partner. The consortium's other partners are Austrian-based OMV Gas International, Hungarian-based MOL, Bulgarian-based Bulgargaz Holding, Romanian-based Transgaz, and BOTAS, which is headquartered in Turkey. Each of the companies holds a 16.67% stake. The plan is to construct a 3,300 km-long pipeline, which will run from Turkey via Bulgaria, Romania and Hungary to Austria. It will connect the major gas reserves of the Caspian region, the Near and Middle East, and other regions with the European market in 2013. Nabucco should thus make a key contribution to Europe's security of supply and promoting competition on the international gas market.

1.4 Notes on reporting

Segment structure in fiscal 2007. The presentation of our business trend in 2007 is structured according to the three following segments: RWE Power, RWE Energy and RWE npower. The RWE upstream subsidiary RWE Dea is a business unit of RWE Power. RWE Trading has also been assigned to RWE Power, as part of the Power Generation Business Unit. We are reporting on RWE Gas Midstream, which was established as of January 1, 2007, under "Other, consolidation" as part of the RWE Energy Division.

American Water stated as "Discontinued operation" in 2007. In line with our intention to float American Water, we state this company in the 2007 consolidated financial statements as a "Discontinued operation." Therefore, figures for the US-based water utility (Water Division) are no longer included in revenue, EBITDA, the operating result, the non-operating result, the financial result, or taxes on income. Prior-year figures have been adjusted accordingly, in compliance with IFRS. However, American Water is still recognized on the balance sheet and cash flow statement (including capital expenditure).

Minor adjustments within RWE Energy. We introduced "Supraregional operations," a new business unit within RWE Energy, with retroactive effect as of January 1, 2006. It mainly includes the former reporting item "Electricity & Gas Transmission" and the activities of Thyssengas and RWE Aqua which used to be stated under "Other, consolidation" within RWE Energy. We have assigned RWE Transgas' sales and transit businesses to "International regions" and subsumed the Czech transmission grid and storage activities under "Supraregional operations." The RWE Solutions Group has been retrospectively reclassified to "Other, consolidation" within RWE Energy in the 2007 consolidated financial statements. Its subsidiaries were deconsolidated in the third quarter of 2006, with a few exceptions.

New reporting structure starting in 2008. Fiscal 2008 is characterized by the pooling and streamlining of Group operations. As explained on page 42, this year, we will combine RWE Trading and RWE Gas Midstream to form a new company called RWE Supply & Trading. Furthermore, the new company RWE Innogy, to which we will transfer nearly all our renewable energy activities, was launched on February 1, 2008. Our reporting will reflect these changes from 2008 onwards. We have adjusted it in line with the segment structure. For further information on this, please turn to page 106 in the chapter entitled "Outlook for 2008."

1.5 Business performance

Electricity production by primary energy source Billion kWh	RWE Power[1]		RWE npower[2]		RWE Group[3]	
	2007	2006	2007	2006	2007	2006
In-house generation	178.9	184.0	33.8	36.5	216.1	223.7
Lignite	76.1	72.9	-	-	76.1	72.9
Hard coal	55.3	50.1	15.1	20.8	71.0	71.6
Nuclear	32.1	47.3	-	-	32.1	47.3
Gas	10.1	8.7	17.7	14.4	29.3	24.3
Renewable energies	3.2	3.0	0.8	0.6	5.2	4.8
Pumped storage, oil, other	2.1	2.0	0.2	0.7	2.4	2.8
Electricity purchased from third parties	-	-	23.7[4]	23.5[4]	108.2	106.1
Total	**178.9**	**184.0**	**57.5**	**60.0**	**324.3**	**329.8**

1 Including electricity procured from power plants not owned by RWE that we can deploy at our discretion on the basis of long-term agreements. At the end of 2007, they break down into 36.3 million kWh (hard coal), 0.9 billion kWh (renewables) and 1.8 billion kWh (pumped storage, oil, other).
2 The item "Renewable energies" includes electricity procured from wind power plants owned by a joint venture in which RWE npower holds a 33% stake. In fiscal 2007, this amounted to 0.7 billion kWh.
3 Including generation and electricity purchases of RWE Energy's regional companies.
4 Electricity purchased by RWE npower largely via RWE Trading.

Electricity generation down due to Biblis power plant outage. In the financial year that just came to a close, the RWE Group produced 216.1 billion kWh of electricity—3% less than in 2006. In-house generation and power purchases combined for 324.3 billion kWh in total electricity production. This was slightly less than in fiscal 2006. In the year under review, 35% of electricity generation was based on lignite, 33% on hard coal, 15% on nuclear, and 14% on gas. Renewables' share amounted to 2%.

RWE Power contributed 178.9 billion kWh of the RWE Group's total in-house electricity production; this represents a share of 83%. This includes electricity generated from power plants not owned by RWE that we can deploy at our discretion on the basis of long-term agreements.
RWE Power generated 3% less electricity than in fiscal 2006. This was primarily due to unplanned outages at both our nuclear power plant units in Biblis, Germany. They were caused by the faulty installation of screw anchors. Block A was offline from September 2006 to February 2008, and Block B was out of operation from October 2006 to November 2007. We replaced the production shortfall with purchases made on the wholesale market and by stepping up the use of our German hard coal-fired power plants. In line with the nuclear consensus reached with the German government, the existing generation allowance for Biblis will not be affected by the outages. The shutdown of the units envisioned by the German Nuclear Energy Act will be postponed accordingly. Since Biblis was offline, our nuclear-based electricity generation was substantially down on the previous year's level, declining by 32%. This was contrasted by increases in production from other fuels. RWE Power generated 10% more electricity from hard coal and 16% more from gas. This was partially due to favourable conditions on the German market. Lignite-based generation was up 4%. This was a result of improved power plant availability, following a production outage caused by a fire at our site in Niederaussem, Germany, in 2006 and planned maintenance work in

the same year. RWE Power's renewable generation output increased by 7%. Most importantly, our run-of-river power plants produced more electricity than in the prior year, because rivers had higher water levels due to substantial rainfall.

RWE npower generated 33.8 billion kWh of electricity—down 7% year on year. In the UK market, high fuel prices meant that hard coal and oil-fired generation was less competitive and generation from these energy sources was down by 27% and 73%, respectively. In contrast, we made more use of our UK-based gas-fired power stations, predominantly because of lower gas prices. Our UK gas power plants increased production by 23%. Renewable output was also up 23%. This is a result of the continued expansion of our installed wind power generation capacity. Furthermore, it was much windier than in the previous year.

RWE Energy made a small contribution of 3.4 billion kWh to total power produced. This output is largely attributable to our German regional companies. It mainly consists of gas-based and hydroelectric power.

The RWE Group's power purchases from third parties advanced by 2% to 108.2 billion kWh, partially because more electricity was fed into RWE Energy's grid in line with the German Renewable Energy Act.

Power plant capacity by primary energy source as of 12/31/2007 in MW	RWE Power[1]		RWE npower[2]	RWE Group[3]	
	Total	Germany		Total	Germany
Hard coal	9,483	9,483	4,481	14,064	9,583
Lignite	10,738	10,041	-	10,755	10,041
Nuclear	6,295	6,295	-	6,295	6,295
Gas	3,917	3,917	2,918	7,098	4,179
Renewable energies	744	525	325	1,348	804
Pumped storage, oil, other	2,343	2,343	2,483	4,973	2,490
Total	**33,520**	**32,604**	**10,207**	**44,533**	**33,392**

1 Including capacities of power stations not owned by RWE that we can deploy at our discretion on the basis of long-term agreements, totalling 6,507 MW (hard coal), 135 MW (renewable energies) and 2,126 MW (pumped storage, oil, other) in fiscal 2007.
2 Including wind power plants with a total installed capacity of 256 MW owned by a joint venture in which RWE npower holds a 33% stake. We have access to electricity generated by these plants on the basis of long-term power supply agreements.
3 Including RWE Energy's generation capacity.

Our 45 gigawatts put us among Europe's leading power producers. At the end of the 2007 financial year, the RWE Group had an installed capacity of 44.5 gigawatts (GW). We thus rank fourth among Europe's power utilities. These figures include the contractually secured capacities mentioned earlier that are not owned by RWE. Our electricity generation capacity increased marginally compared with 2006. This is in part due to a new 249-MW gas topping turbine that was commissioned in our lignite-fired power plant in Weisweiler near Cologne, Germany. Hard coal accounts for the biggest share of our installed capacity at 32%, followed by lignite (24%), gas (16%) and nuclear power (14%). Renewable energy had a share of 3%. The geographical focus of our electricity generation is Germany: This is where 33.4 GW, or 75%, of our power plant capacity is located. In second place, with 10.2 GW, or 23%, of our capacity is the UK. Hungary comes in third, with a production capacity of 0.7 GW, or 1.6%.

Emissions balance 2007 million metric tons	Germany[1]	UK	Other	RWE Group
CO_2 emission	157.8	22.0	7.3	187.1
Free allocation of CO_2 certificates	144.7	17.0	8.1	169.8
Shortage of CO_2 certificates	**13.1**	**5.0**	**-0.8**	**17.3**

1 Includes power stations not owned by RWE that we can deploy at our discretion on the basis of long-term agreements. In the year under review, they produced 34.6 million metric tons of CO_2 and were allocated certificates for 27.1 million metric tons.

Emissions balance and purchase of CO_2 certificates for electricity generation. In fiscal 2007, our electricity generation operations emitted 187.1 million metric tons of carbon dioxide. RWE-owned power plants accounted for 152.5 million metric tons, and the remaining 34.6 million metric tons come from contractually secured capacity in Germany. CO_2 emissions were up by 8.8 million metric tons compared with 2006. In Germany, emissions rose by 11.1 million to 157.8 million metric tons. This is because we increased coal- and gas-based generation, while CO_2-free power production from nuclear plants decreased considerably owing to the Biblis outage. In contrast, our carbon dioxide emissions in the UK declined by 2.7 million to 22.0 million metric tons, because RWE npower's hard coal and oil power plants had low capacity utilization. In Hungary, we emitted 6.6 million metric tons, which was marginally higher than the previous year's level.

In the year under review, we received free state allocations of certificates equal to 169.8 million metric tons of CO_2. This is 17.3 million metric tons less than our emissions. In Germany, we received certificates corresponding to 144.7 million metric tons, while in the UK, the allocation represented 17.0 million metric tons. This resulted in shortfalls of 13.1 million metric tons and 5.0 million metric tons, respectively. In Central Eastern Europe, we were allocated slightly more emissions allowances than we needed. We were able to use these certificates in other countries.

Gas production up, oil production down. In the fiscal year that just ended, RWE Dea, our upstream company, produced 3,215 million m^3 of gas and 2,749 thousand m^3 of oil. In terms of oil equivalent, production totalled 36.9 million barrels. In the previous year, it had amounted to 42.1 million barrels. Gas production increased by 8%. This was mainly a result of our starting production in several UK North Sea gas fields. Conversely, in Germany, we produced less gas year on year. Lower demand caused by the weather played a role. Oil production fell 28%. This was in part due to the fact that we sold our stake in Kazgermunai in Kazakhstan in July 2006 and our concession in Dubai in April 2007. Another factor was that shares in oil production from the Snorre oilfield in Norway held by consortium partners were re-determined in accordance with the contract. This decreased our share of production. We have to refund all the past excess production allocations using our current production by the end of 2008.

Electricity sales slightly below year-earlier level. In fiscal 2007, we sold 306.4 billion kWh of electricity to external customers—2 % less than in 2006. Electricity sales are typically somewhat lower than the amount of power generated and purchased. This is due to grid losses as well as our in-house consumption by lignite production and pumped-storage power plants.

External electricity sales volume by customer segment Billion kWh	RWE Power[1]		RWE Energy		RWE npower		RWE Group	
	2007	2006	2007	2006	2007	2006	2007	2006
Private and commercial customers	0.3	0.4	37.5	38.2	22.3	22.3	60.4	61.1
Industrial and corporate customers	-	2.3	65.8	58.5	32.4	34.1	98.2	94.9
Distributors	14.3	13.7	65.0	62.0	-	-	79.3	75.7
Electricity trading	68.5	80.4	-	-	-	-	68.5	80.4
Total	**83.1**	**96.8**	**168.3**	**158.7**	**54.7**	**56.4**	**306.4**	**312.1**

1 Including RWE Trading.

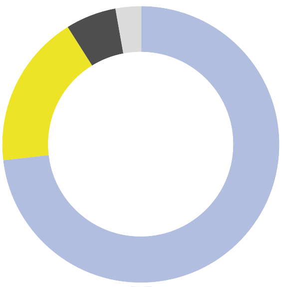
RWE Power generated external sales of 83.1 billion kWh of electricity. Electricity sales of 68.5 billion kWh were allocable to sales of in-house power production on the wholesale market via RWE Trading. The figures do not include pure trading transactions with electricity procured from third parties. Compared with 2006, sales volume dropped by 14%, in part due to the outages at both our nuclear power plant units in Biblis, Germany.

Sales by RWE Energy amounted to 168.3 billion kWh—up 6% on 2006. Most significantly, there was a rise in sales of electricity fed into our grid in compliance with the German laws for the promotion of renewables-based energy (Renewable Energy Act) and combined heat and power generation (CHP Act), which was fed into our grid. New contracts with industrial key accounts and power utilities contributed to the rise. The good economic trend was another factor. In contrast, there was a decline in sales in business with private and small commercial customers. This is in part due to energy savings realized by consumers. Furthermore, our customer figures were slightly down as a result of rising churn rates.

As of December 31, 2007, RWE Energy and its subsidiaries supplied 15.5 million customers with electricity. In the preceding year, this figure had amounted to 15.8 million. The decline is attributable to Germany, our main market, where the customer base decreased from 11.9 million to 11.5 million. This was partially a result of the sale of our minority stake in Stadtwerke Wuppertal. Furthermore, we felt the consequences of the increasingly fierce competition in the German electricity sales sector. Approximately 350,000 of our customers opted for a new supplier in 2007. But some of the contract terminations take effect in 2008. We managed to win 100,000 customers. eprimo was very successful in acquiring customers. By year-end, the company had a household customer base of 200,000. RWE's "Treuestrom" offering was very well received. It guarantees a fixed rate for three years. By the end of the year under review, 100,000 households had already opted for this innovative model contract. Our shares of the Central Eastern European market remained stable. We served 2.1 million customers in Hungary, 0.9 million in Poland, and 0.6 million in Slovakia.

In the fiscal year that just ended, RWE npower's electricity sales totalled 54.7 billion kWh. This was 3% less than the high level achieved a year earlier. Weather-related effects reduced the amount of electricity used for air conditioning. This applied especially to the corporate sector. Since UK homes are rarely equipped with air conditioning and electric heating, the mild weather did not significantly affect their electricity consumption.

At the end of the fiscal year, over 4.3 million households and small commercial operations were RWE npower electricity customers. This was roughly on par with the year-earlier level. We have a 16% share of the UK household customer market. The number of industrial and corporate customers was also essentially unchanged, at 103,000.



Electricity sales volume of the RWE Group by region in 2007 (2006) in %

- **73.3** (74.1) Germany
- **17.9** (18.1) UK
- **5.8** (5.1) Hungary
- **3.0** (2.7) Others

External gas sales volume by customer segment Billion kWh	RWE Power[1]		RWE Energy		RWE npower		RWE Group	
	2007	2006	2007	2006	2007	2006	2007	2006
Private and commercial customers	-	-	64.1	70.5	46.2	41.4	110.3	111.9
Industrial and corporate customers	3.1	3.5	103.8	110.4	9.7	8.7	116.6	122.6
Distributors	17.0	21.5	91.1	104.9	-	-	108.1	126.4
Total	**20.1**	**25.0**	**259.0**	**285.8**	**55.9**	**50.1**	**335.0**	**360.9**

1 Including RWE Dea and RWE Trading.

Gas sales volume down 7% year on year due to the weather. In the year under review, RWE sold 335.0 billion kWh of gas to outside customers. This corresponds to a 7% drop compared to 2006. The main driver for the decline was the mild weather.

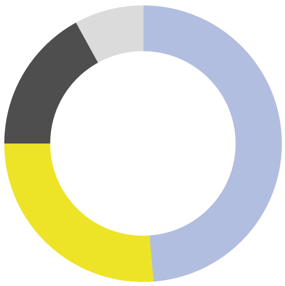
Gas sales generated by RWE Power largely correspond to the quantities RWE Dea produces and sells to distributors and end customers. Sales were also generated by RWE Trading. However, they were substantially down, because we had sold a contract with a key account to another gas supplier at the end of 2006. All in all, the RWE Power Division saw gas sales decrease by 20% to 20.1 billion kWh.

RWE Energy's gas sales declined by 9% to 259.0 billion kWh, largely owing to weather-related effects. This decline is partially due to the cost-conscious behaviour displayed by consumers. Moreover, the year-earlier figure was exceptionally high, in part since RWE Energy sold large volumes of power plant gas.

At the end of the year, RWE Energy and its subsidiaries served 7.6 million gas customers. This represents a decrease of 0.1 million and was largely due to the sale of the stake in Stadtwerke Wuppertal. The number of customers we served in Germany, which is our main market, thus declined from 3.1 million to 3.0 million. Customers switching suppliers in response to competition did not have a major impact on the bottom line. In contrast, outside Germany, customer churn resulted in marginal gains. In the Czech Republic, we supplied gas to 2.3 million customers at the end of December. In Hungary, we served 2.0 million, with 0.3 million supplied in the Netherlands.

RWE npower sold 55.9 billion kWh of gas, surpassing the year-earlier level by 12%, despite the warmer weather. We benefited from new customer acquisitions—especially in terms of UK households.

At the end of 2007, 2.7 million homes and small commercial enterprises obtained gas from RWE npower—nearly 170,000 more than in the previous year. This was supplemented by 19,600 industrial and corporate customers, which represents a gain of 3,300. We thus have a 12% share of the UK household customer market. We gained customers as a result of our successful brand strategy and improved customer service. The number of customers to whom we supply both electricity and gas also rose. It totalled 2.2 million, as compared to 2.1 million at the end of the previous year.



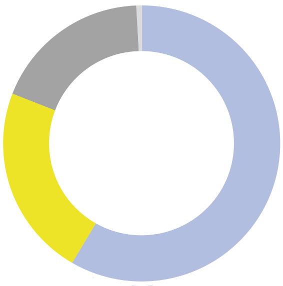
Gas sales volume of the RWE Group by region 2007 (2006) in %

- **49.0** (51.0) Germany
- **26.0** (26.7) Czech Republic
- **17.0** (15.5) UK
- **8.0** (6.8) Others

External revenue € million	2007	2006	+/– in %
RWE Power	6,595	6,574	0.3
Power Generation[1]	5,099	4,855	5.0
RWE Dea	1,496	1,719	-13.0
RWE Energy[2]	26,900	27,398	-1.8
German regions	16,015	16,309	-1.8
International regions	5,589	5,510	1.4
Supraregional operations	5,012	4,555	10.0
Other, consolidation	284	1,024	-72.3
RWE npower	8,920	8,485	5.1
Other, consolidation	92	97	-5.2
RWE Group	**42,507**	**42,554**[3]	**-0.1**
of which:			
Electricity revenue	27,917	25,771	8.3
Direct electricity tax	961	971	-1.0
Gas revenue	10,768	12,055	-10.7

1 Including RWE Trading.
2 Regional structure adjusted; see commentary on page 60.
3 Figure adjusted; the Water Division, which is stated under “Discontinued operations,” is no longer included.

RWE Group revenue by region in 2007 (2006[1]) in %



58.4	(62.5)	Germany
22.5	(21.1)	UK
18.5	(15.2)	Rest of Europe
0.6	(1.2)	Others

1 Figures adjusted; see commentary on page 60.

Organic revenue up 2%. In the year under review, the RWE Group generated €42.5 billion in external revenue. As already explained on page 60, figures for American Water are no longer included in revenue for 2006 or 2007. External revenue was flat compared with the previous year and was thus slightly lower than expected. In the forecast we published in February 2007, we had anticipated a slight increase. However, we had assumed that gas consumption and gas prices would be higher than they actually were. Some €700 million in revenue was lost due to the sale of RWE Solutions in August 2006. Currency effects did not play a significant role. Sterling lost in value averaged over the year, dropping from £0.68/€ to £0.69/€. This reduced revenue by €70 million. In organic terms, i.e. net of consolidation and currency effects, consolidated revenue was 2% up year on year. This was partially due to higher prices and increased sales in the German end customer electricity business.

The following is an overview of the development of revenue by division:

External revenue posted by RWE Power was essentially unchanged at €6,595 million. The Power Generation Business Unit (including RWE Trading) recorded a gain of 5%, largely driven by RWE Trading's coal trading activities. We realized high prices when selling RWE Power's electricity output on the wholesale market to third parties. But sales significantly decreased, in part due to the Biblis outage. RWE Dea saw external revenue decrease by 13% to €1,496 million. Gas sold by our upstream subsidiary realized lower prices than in 2006—above all in the UK. Another factor was the decline in oil production.

External revenue generated by RWE Energy fell by 2% to €26.9 billion, in part due to the sale of subsidiaries of RWE Solutions. Gas revenue posted by the division experienced a drop of 15% to €8.3 billion. Weather-induced sales shortfalls had an impact here. In the electricity business, RWE Energy posted a gain of 11% to €17.6 billion. Drivers were the volume effects explained earlier and above all the impact of prices. Most of our German regional companies, including RWE Rhein-Ruhr and RWE Westfalen-Weser-Ems, raised their general tariffs for households and small commercial customers as of January 1, 2007, or later in the year. Prices had to be adjusted in the other customer segments as well. This was due to a rise in power procurement costs and mounting burdens stemming from the German Renewable Energy Act.

The RWE npower Division grew external revenue by 5% to €8,920 million. Electricity revenue rose from €6,174 million to €6,449 million, and gas revenue increased from €1,777 million to €2,092 million. At the end of April 2007, due to competition, RWE npower reduced tariffs in the electricity and gas sales businesses by an average of 3% and 16%, respectively. However, this was contrasted by revenue-enhancing effects arising from tariff increases as of April 1, 2006, and October 1, 2006. Furthermore, we acquired new customers. Weather-induced reductions in sales volume dampened the rise in revenue.

EBITDA € million	2007	2006	+/– in %
RWE Power	4,426	3,372	31.3
Power Generation[1]	3,671	2,574	42.6
RWE Dea	755	798	-5.4
RWE Energy[2]	2,742	3,177	-13.7
German regions	1,552	1,856	-16.4
International regions	760	684	11.1
Supraregional operations	833	868	-4.0
Other, consolidation	-403	-231	-74.5
RWE npower	870	658	32.2
Other, consolidation	-136	-35	-288.6
RWE Group	**7,902**	**7,172**[3]	**10.2**

1 Including RWE Trading.
2 Regional structure adjusted; see commentary on page 60.
3 Figure adjusted; the Water Division, which is stated under “Discontinued operations,” is no longer included.

Reconciliation of income from operating activities to EBITDA € million	2007	2006[1]	+/– in %
Income from operating activities	5,774	4,561	26.6
+ Income from investments	597	790	-24.4
– Non-operating result	149	330	-54.8
Operating result	6,520	5,681	14.8
– Operating income from investments	-541	-386	-40.2
+ Operating depreciation and amortization	1,923	1,877	2.4
EBITDA	**7,902**	**7,172**	**10.2**

1 Figure adjusted; the Water Division, which is stated under “Discontinued operations,” is no longer included.

Double-digit year-on-year rise in operating result and EBITDA. Despite the adverse effects of German grid regulation and the outage of the Biblis nuclear power plant, the RWE Group further improved earnings in 2007. The main reasons for this were the positive organic trend displayed by our power generation business and an exceptionally good trading result. EBITDA grew by 10% to €7,902 million. It was thus at the upper end of the prognosis we had published in February 2007. The operating result advanced 15% to €6,520 million. We thus exceeded the forecast, which had predicted an increase in the order of 10%. On balance, consolidation and currency effects only had a minor impact on the development of earnings. Net of these effects, EBITDA would have been up 11% and the operating result would have gained 17%.

Operating result € million	2007	2006	+/– in %
RWE Power	3,706	2,744	35.1
Power Generation[1]	3,214	2,132	50.8
RWE Dea	492	612	-19.6
RWE Energy[2]	2,296	2,506	-8.4
German regions	1,209	1,427	-15.3
International regions	692	583	18.7
Supraregional operations	767	714	7.4
Other, consolidation	-372	-218	-70.6
RWE npower	724	512	41.4
Other, consolidation	-206	-81	-154.3
RWE Group	**6,520**	**5,681**[3]	**14.8**

1 Including RWE Trading.
2 Regional structure adjusted; see commentary on page 60.
3 Figure adjusted; the Water Division, which is stated under “Discontinued operations,” is no longer included.

The following is an overview of our operating result by division:

RWE Power improved its operating result by 35% to €3,706 million. The breakdown by business unit is as follows:

- Power Generation: The operating result recorded by this business unit rose by 51%. This was primarily due to the fact that prices we realized for our electricity production were higher than in 2006. As mentioned earlier, we had already largely sold forward our 2007 electricity generation in prior years. The average price of these contracts was significantly higher than the previous year’s corresponding figure (see page 48). However, we were adversely affected by the outage of the Biblis nuclear power plant. In 2007, the shortfall amounted to some €810 million, as compared to €280 million a year earlier. Steps taken to modernize our power plant portfolio caused costs to rise as well. Our decision not to build the dual-unit hard coal power plant we had envisioned for Ensdorf, Germany, due to the lack of local public acceptance also had a negative impact on the result. This is because expenses had already been incurred for the project. In addition, costs were incurred to cancel contractual obligations. The cost of purchasing CO_2 emissions allowances amounted to €160 million, which was twice as much as in the previous year. This was due to the increased use of our hard coal power plants. The 2007 financial year was extraordinarily successful for RWE Trading, which we report as part of the Power Generation Business Unit. The company closed the year under review with an operating result of €592 million (previous year: €153 million). Gains were achieved especially in gas trading and in Continental European electricity trading.

- RWE Dea: The operating result of our oil and gas upstream activities was 20% down year on year. This was mainly due to the absence of the operating result from our stake in Kazgermunai in Kazakhstan, which was sold, the decline in our share of production in the Snorre oilfield in Norway, and higher exploration costs. A positive effect was felt from the rise in our gas production and higher oil prices.

The operating result recorded by RWE Energy dropped by 8% to €2,296 million. The main reason for this was the onset of regulation in the German electricity and gas business, which affected the full year in 2007 for the first time. It resulted in a burden of approximately €500 million compared with fiscal 2006. Cost reductions and the absence of last year's negative one-off effects had a counteracting impact. RWE Gas Midstream, which took up operations as of January 1, 2007, and which we still stated as part of RWE Energy under "Other, consolidation" in the year under review, recorded an operating loss of €59 million. This was due to start-up costs. The following is a breakdown of the operating result by business unit:

- German regions: RWE Energy's domestic regional companies closed fiscal 2007 with an operating result that was 15% lower year on year, above all owing to the regulator's grid fee cuts imposed on our electricity and gas distribution business. The weather-induced decline in our gas sales also had a negative effect. Furthermore, we have not yet been able to fully pass through the rise in electricity purchasing costs resulting from the added burdens stemming from the German Renewable Energy Act, among other things. Measures taken to reduce costs and enhance efficiency limited the decrease in earnings.

- International regions: The operating result of our Continental European sales and distribution grid activities outside Germany grew by 19%, despite weather-induced shortfalls in gas sales. This was largely due to one-off effects.

- Supraregional operations: The operating result recorded by this business unit was up 7% year on year, despite the substantial grid fee cuts on our German electricity transmission business by the regulator. The basis for this growth was cost-cutting measures and successes in acquiring new customers by RWE Key Account as well as wider margins in the Czech gas transmission business. Furthermore, income earned by our investment in Berlinwasser improved.

RWE npower posted an operating result of €724 million. This represents an increase of 41% compared with 2006. The strong growth was mainly driven by electricity generation, where we realized much higher prices. Furthermore, we benefited from the expiry of older power supply agreements with low margins. An adverse effect was felt from the increase in operating costs. The cost of purchasing CO_2 emissions certificates fell by €59 million to €114 million. This was due to the decline in RWE npower's emissions and the lower price of certificates. We benefited from customer acquisitions in RWE npower's supply business. But this was contrasted by narrower margins in the household customer segment caused by higher gas and electricity procurement costs and higher transmissions fees for both products. In addition, costs incurred for customer service increased.

Key figures for value management [1] in fiscal 2007	Operating result € million	Capital employed[2] € million	ROCE in %	Capital costs before taxes in %	Relative value added in %	Absolute value added in 2007 € million	Absolute value added in 2006 € million
RWE Power[3]	3,706[4]	15,349	24.2	10.5	13.7	2,105	1,188
RWE Energy	2,296	20,844	11.0	9.0	2.0	420	586
RWE npower	724	6,424	11.3	10.0	1.3	82	-153
Other, consolidation	-206	-2,907	-	-	-	350	453
RWE Group	**6,520[4]**	**39,710**	**16.4**	**9.0**	**7.4**	**2,957**	**2,074**

1 Capital employed was determined using a new method (see commentary on pages 73 and 208 et seq.). This leads to lower figures for ROCE and value added. Prior-year figures were adjusted accordingly.
2 Averaged for the year.
3 Including RWE Dea and RWE Trading.
4 To determine ROCE and value added, one must add €11 million in interest income from lease accounts receivable.

Return on capital employed improved to 16.4%. Our strategy centres on increasing the company's value. Additional value is created when the return on capital employed (ROCE)exceeds the cost of capital. We increased the value of the company considerably in 2007 again. ROCE was 16.4%, clearly surpassing the Group's capital costs of 9.0% before taxes. This was primarily driven by the positive earnings development.

We have explained how we determine our value-management parameters on page 208 et seq. We have refined the concept's methodology. In 2007, depreciable non-current assets are no longer stated at carrying amounts. Instead, we recognize them at half of their historic costs. The advantage of the new method is that the determination of ROCE is no longer influenced by the age of the assets. This reduces the fluctuation in return caused by the investment cycle. Due to the switch in methodology, the RWE Group now states a much higher level of capital employed and, accordingly, lower returns. To ensure comparability to prior-year figures, we adjusted them accordingly.

Value added is the central controlling instrument for all of the RWE Group's activities. It is obtained by multiplying the difference between ROCE and capital costs by capital employed. According to the new method, RWE Group's value added for the 2007 financial year amounts to €2,957 million. This is €883 million more than in 2006.

The following is an overview of the development of value added by division:

- Value added by RWE Power totalled €2,105 million, representing the largest contribution within the RWE Group. This was an increase of €917 million year on year, and was due to the improved earnings of our German power generation operations and the extraordinarily positive trading result. Substantial investments made by the division had a negative impact on value added. This caused capital employed to increase immediately, whereas in some cases, the positive effects on earnings will only be felt in later years when the new plants are commissioned.

- RWE Energy made a value contribution of €420 million. This is €166 million less than in 2006. The single-most important effect was the impact of fee cuts in the German grid business.

- In the fiscal year being reviewed, RWE npower was able to earn its cost of capital for the first time. The UK energy company achieved €82 million in value added. This is an increase of €235 million over fiscal 2006, which mainly results from the improved earnings generated by the power generation business. The rise in capital expenditure led to counteracting effects. RWE npower would have earned its cost of capital even if the method for determining capital employed had not changed. Based on the old approach, value added would have amounted to €40 million (previous year: –€185 million).

Non-operating result € million	2007	2006[1]	+/– € million
Capital gains	339	474	-135
Impairment losses	0	-6	6
Restructuring, other	-488	-798	310
Non-operating result	**-149**	**-330**	**181**

1 Figures adjusted; see comments on page 60.

Reconciliation to net income characterized by negative one-off effects. In line with the forecast we published in February 2007, net income declined considerably. In 2006, the successful sale of Thames Water and a change in tax law had led to an especially high figure. The decrease in 2007 was limited by the positive development of earnings as well as by improvements in the non-operating and financial results.

The non-operating result was negative, amounting to -€149 million, but was significantly up on the comparable figure for 2006 (-€330 million). Its components developed as follows:

- Capital gains amounted to €339 million. They largely stem from the divestment of our Dutch gas grid activities, which we sold to the City of Eindhoven effective June 1, 2007. The transfer of a 25% stake in rhenag Rheinische Energie AG to RheinEnergie AG also had a positive effect. Despite the aforementioned transactions, capital gains were down year on year. This was mainly due to the high contribution obtained from the sale of our 25% stake in the oil production company Kazgermunai in 2006.

- No impairment losses were recognized for continuing operations in the period under review.

- The result stated under "Restructuring, other" amounted to -€488 million—up €310 million on the corresponding figure in 2006, which reflected substantial one-off negative effects. Amongst other things, in 2006, we had accrued provisions to limit the negative impact on earnings from German grid regulation. But special items had a negative effect on the non-operating result in 2007 as well. Expenses incurred by RWE npower prior to its acquisition by RWE in 2002 became tax-deductible retroactively. Under IFRS, this had two effects. On the one hand, there was a lower tax charge for the Group in 2007. On the other hand, a retroactive adjustment was made to the goodwill stemming from the acquisition of the UK energy company in 2002. The non-operating result was thus reduced by €138 million. Another negative effect was felt from the build-up of provisions to cover liability risks concerning a non-core activity that we sold several years ago. We amortized RWE npower's customer base by €325 million (2006: €327 million). Changes made to nuclear provisions led to €178 million in income (2006: €164 million).

Financial result € million	2007	2006[1]	+/– in %
Interest income	855	2,201	-61.2
Interest expenses	-1,334	-2,710	50.8
Net interest	**-479**	**-509**	**5.9**
Interest accretion to non-current provisions	-771	-1,136	32.1
Other financial result	112	-169	166.3
Financial result	**-1,138**	**-1,814**	**37.3**

1 Figures adjusted; see comments on page 60.

The financial result improved by €676 million to -€1,138 million. The increase in cash and cash equivalents due to the sale of Thames Water was a main contributor. However, the resulting effects are not directly evident, since the financial result's individual items are significantly affected by the contractual trust arrangement (CTA) described on page 58. On balance, our net interest posted a slight improvement. Opposing effects came to bear here. Interest income decreased through the transfer of assets via the CTA, whereas the reduction in debt resulting from the sale of Thames Water had a positive impact. The decline in provisions for pensions led to a decrease in the interest accretion to non-current provisions. Furthermore, the deconsolidation of special funds implemented via the CTA generated €155 million in non-recurrent income, which we have subsumed under the "Other financial result." The increase in our financial result is also partially due to the fact that our exchangeable bond on shares in Heidelberger Druckmaschinen, which was issued in 2004, came due in the year under review and that we reduced our stake in the company (€142 million).

Our continuing operations generated income before tax amounting to €5,233 million. This is 48% more than in 2006.

The effective tax rate increased significantly, rising to 40%. In the previous year, it was an exceptionally low 27% owing to a one-off effect: Due to a change in German tax law, RWE had to capitalize its corporate tax credit of €636 million with a positive effect on earnings. Special items influenced the effective tax rate in fiscal 2007 as well. As a result of the German 2008 corporate tax reform, our average income tax rate in Germany dropped to about 31% as of January 1, 2008. This resulted in a recalculation of deferred taxes carried on the balance sheet, which led to a one-off cost of €256 million. Tax reductions in the UK and the Czech Republic produced counteracting effects. The restatement of deferred taxes resulted in €41 million and €25 million in non-recurrent income, respectively. In addition, RWE npower benefited from the tax revenue mentioned on page 74.

Income from continuing operations after tax rose 23% to €3,157 million. Income from discontinued operations declined from €1,442 million to -€274 million. In the year under review, this item exclusively included American Water. Fiscal 2006's comparable figure also included recurrent income from Thames Water (€330 million) and the deconsolidation result achieved by selling the company (€991 million). In the fourth quarter of 2007, we subjected the fair value of American Water carried on the balance sheet to an impairment test. An impairment of €429 million was recognized since the fair value less expected costs to sell was below the carrying amount. Excluding the aforementioned fair value adjustment, income after tax earned by American Water amounted to €155 million, which was much higher than the €104 million achieved in the previous year. The minority interest increased by €58 million to €224 million.

Net income recorded by the RWE Group dropped by 31% to €2,659 million. Earnings per share declined from €6.84 to €4.73.

Reconciliation to net income		2007	2006[1]	+/– in %
Operating result	€ million	6,520	5,681	14.8
Non-operating result	€ million	-149	-330	54.8
Financial result	€ million	-1,138	-1,814	37.3
Income from continuing operations before tax	€ million	**5,233**	**3,537**	**48.0**
Taxes on income	€ million	-2,076	-966	-114.9
Income from continuing operations	€ million	**3,157**	**2,571**	**22.8**
Income from discontinued operations	€ million	-274	1,442	-119.0
Income	€ million	**2,883**	**4,013**	**-28.2**
Minority interest	€ million	224	166	34.9
Net income[2]	€ million	**2,659**	**3,847**	**-30.9**
Recurrent net income	€ million	**2,977**	**2,466**	**20.7**
Earnings per share	€	4.73	6.84	-30.8
Recurrent net income per share	€	5.29	4.38	20.8
Effective tax rate	%	40	27	–

1 Figures adjusted; see commentary on page 60.
2 RWE shareholders' share in net income.

Recurrent net income improved by 21%. The key figure that is decisive for our dividend policy is recurrent net income. This figure is calculated by subtracting from net income the non-operating result which is affected by one-off effects and major non-recurrent effects on the financial result, taxes, and income from discontinued operations. Accordingly, American Water's goodwill impairment and the 2006 capital gains from the deconsolidation of the sale of Thames Water were not considered in this figure. However, the two companies' recurrent net income was not excluded. In the year under review, recurrent net income totalled €2,977 million. This was 21% more than in 2006. We thus clearly exceeded the forecast we had published in February 2007. We had expected an increase in the order of 10%.

Planned annual efficiency enhancements € million	2007	2008	2009	2010	Total
	100	**100**	**200**	**200**	**600**

Efficiency-enhancement programme is being implemented as planned. The programme we initiated to improve efficiency is on schedule. Plans include measures to reduce costs and increase revenue. This should gradually grow our annual operating result by a total of €600 million by the end of 2010. One of the points of focus is to enhance the performance of our German electricity and gas grid business. The aim is to at least partially compensate for the effect of the fee cuts mandated by the grid regulator. In addition, we plan to take comprehensive measures to improve the technical availability of our power plants. We had intended to achieve an earnings contribution of about €100 million for fiscal 2007 with the programme. This target was achieved. We are in the process of identifying further savings potential in the coming years and have begun to analyze our key business processes extensively to this end. We expect to be able to expand the efficiency-enhancement programme considerably this year.

Capital expenditure on property, plant and equipment € million	2007	2006	+/– € million
RWE Power[1]	1,635	1,302	333
RWE Dea	505	477	28
RWE Energy	1,147	1,174	-27
RWE npower	587	396	191
Water Division	635	1,584	-949
Other, consolidation	61	38	23
RWE Group	**4,065**	**4,494**	**-429**

1 Including RWE Trading.

Capital expenditure in the energy business up 18%. In the year under review, we spent €4,227 million in capital. This represents a decline of 11% compared with 2006 (€4,728 million). Capital expenditure on property, plant and equipment decreased by 10% to €4,065 million. The decline is mainly attributable to the Water Division and results from the fact that the figure for 2006 still includes capital spent by Thames Water. Capital expenditure by all of the other divisions rose by 18% to €3,430 million. Additional capital was spent above all on the construction of new power plants. However, we did not progress with these projects as rapidly as planned, in part due to delays in approval procedures. We decided not to go ahead with the power station project in Ensdorf, Saarland/Germany, (see page 55). Therefore, capital expenditure on property, plant and equipment in the energy business fell shy of the €4 billion included in the forecast we published in February 2007. Capital expenditure on financial assets was low, coming in at €162 million.

Capital expenditure on financial assets € million	2007	2006	+/– € million
RWE Power[1]	67	5	62
RWE Dea	-	4	-4
RWE Energy	56	287	-231
RWE npower	-	11	-11
Water Division	9	4	5
Other, consolidation	30	-73	103
RWE Group	**162**	**234**	**-72**

1 Including RWE Trading.

The following is an overview of investing activity by division:

Capital spending by RWE Power amounted to €1,702 million—up €395 million on the previous year. Most of this money was spent on property, plant and equipment. The major projects were the 2,100-MW dual-block lignite-fired power plant in Neurath near Cologne, Germany, and the 875-MW combined-cycle gas turbine power station in Lingen, Germany. Both these facilities are under construction. Furthermore, we did preparatory work on the construction of the hard coal dual blocks in Hamm, Germany, and Eemshaven, Netherlands. Capital already spent on the hard coal twin unit in Ensdorf, Germany, was recognized as a cost, owing to the cancellation of the project. Capital expenditure by RWE Dea rose by €24 million to €505 million. It was earmarked for the expansion of gas production in North Africa and the UK, among other things.

RWE Energy's capital expenditure amounted to €1,203 million compared with €1,461 million a year earlier. Whereas capital expenditure on financial assets was markedly down, capital expenditure on property, plant and equipment essentially remained unchanged. One of the key areas of investing activity were the grid connections for new power plants. Funds were also dedicated to modernizing high and medium-voltage lines as well as transformer stations. Furthermore, we had to repair damage caused by Hurricane Kyrill at the beginning of 2007. RWE Energy channelled some 80% of its capital expenditure on property, plant and equipment to the expansion and modernization of our grid infrastructure. Capex in the gas business was primarily used to increase storage capacity.

RWE npower spent €587 million on investments, which was significantly more than the €407 million spent in the previous year. Capital expenditure was exclusively on property, plant and equipment. The biggest project was the construction of the 1,650-MW gas-fired power plant in Staythorpe, UK, which began in 2007. In addition, we did preparatory work for the planned 2,000-MW gas-fired power station in Pembroke, UK. Further funds were spent to increase installed renewable energy capacity. One such investment was made in the construction of the 90-MW Rhyl Flats offshore wind farm off the coast of Wales, which is scheduled for completion in 2009. Moreover, RWE npower spent capital on retrofitting the Aberthaw hard coal-fired power plant with a flue gas desulphurization unit.

The Water Division's capital expenditure totalled €644 million. The €1,588 million recorded in the previous year was much higher, because it still included Thames Water for eleven months. Capital spent in the year under review was mainly dedicated to improving the water pipe infrastructure in our North American supply areas.

Workforce[1]	12/31/07	12/31/06	+/– in %
RWE Power[2]	18,840	18,467	2.0
RWE Energy	28,472	28,418	0.2
RWE npower	11,975	11,624	3.0
Other[3]	4,152	3,216	29.1
RWE Group	**63,439**	**61,725**	**2.8**
Germany	38,283	37,782	1.3
Outside Germany	25,156	23,943	5.1

1 Converted to full-time positions. The Water Division, which has been stated as a "discontinued operation," is not included. As of December 31, 2007, this division had 7,051 employees (previous year: 6,809).
2 Including RWE Dea and RWE Trading.
3 Including RWE Systems.

Employee headcount up 3%. As of the balance-sheet date, the RWE Group employed 63,439 people (converted to full-time positions). This was 1,714, or 3%, more than in the previous year. These figures do not include American Water, since we state the company as a "discontinued operation." Company acquisitions and disposals did not have a significant effect on the number of employees. Operating staff changes added 1,730 employees, 517 of whom work in Germany. RWE npower recorded significant increases in sales and customer service. However, the UK energy company transferred some 800 employees to our newly established service subsidiary, RWE Systems UK, which we report under "Other." RWE Power created numerous new jobs, too. As in prior years, in 2007, we trained far more people than we needed. By the end of the year under review, 2,918 young adults were in a professional training programme at RWE. Staff figures do not include trainees.

Procurement structures further improved. With the exception of raw materials sourcing, our purchasing operations are coordinated by our internal service provider RWE Systems. We work with a modern supplier management system that creates transparency throughout the Group and allows us to focus on the suppliers with the most favourable conditions. Besides enabling us to gain economies of scale, this allows us to optimize the procurement processes themselves. The cornerstones of our supplier management system are the Group purchasing portal, electronic catalogues, online auctions, and web-based invitations to tender. In 2002, we launched a savings programme aiming to improve the conditions we receive from our suppliers over the long term. Our measures were successful: By the end of 2006, we had realized permanent savings of €340 million. In fiscal 2007, we achieved further savings through a new programme.

Raw materials purchasing is handled by RWE Power, RWE Gas Midstream and RWE Trading. In 2007, the amount of hard coal procured to generate electricity totalled 23.3 million metric tons of hard coal units (HCU) (previous year: 23.8 million metric tons). This includes coal used in power plants not owned by RWE that we can deploy at our discretion on the basis of long-term agreements. In the financial year that just ended, RWE Power used 18.1 million metric tons of HCU (previous year: 16.7 million metric tons) and RWE npower purchased 5.2 million metric tons (previous year: 7.1 million metric tons). We cover over 60% of coal demand from our own German hard coal-fired power plants with domestic production. Russia is RWE npower's major supplier. Nearly 70% of the coal used in our UK power plants is imported from Russia. RWE sources lignite from proprietary opencast mines. In the Rhineland, our main mining region, we produced about 100 million metric tons of lignite in 2007 (previous year: 96 million metric tons). Our power plants used 89 million metric tons to generate electricity, and we used 11 million metric tons to manufacture refined products. Our gas procurement activities are pooled under RWE Gas Midstream. Production companies in Russia, Norway and the Netherlands are among the RWE Group's major gas suppliers.

1.6 Key figures by division at a glance

RWE Power[1]		2007	2006	+/– in %
External revenue	€ million	6,595	6,574	0.3
Intra-group revenue	€ million	10,003	8,531	17.3
Total revenue	€ million	16,598	15,105	9.9
EBITDA	€ million	4,426	3,372	31.3
Operating result	€ million	3,706	2,744	35.1
Return on Capital Employed (ROCE)	%	24.2	18.5[2]	-
Weighted average cost of capital (WACC) before tax	%	10.5	10.5	-
Value added	€ million	2,105	1,188[2]	77.2
Capital employed	€ million	15,349	14,928[2]	2.8
Capital expenditure	€ million	1,702	1,307	30.2
Property, plant and equipment	€ million	1,635	1,302	25.6
Financial assets	€ million	67	5	-
		12/31/07	12/31/06	
Workforce[3]		18,840	18,467	2.0

1 Including RWE Dea and RWE Trading.
2 Figures adjusted; see commentary on pages 73 and 208 et seq.
3 Converted to full-time positions.

RWE Energy		2007	2006	+/– in %
External revenue	€ million	26,900	27,398	-1.8
Intra-group revenue	€ million	1,310	748	75.1
Total revenue	€ million	28,210	28,146	0.2
EBITDA	€ million	2,742	3,177	-13.7
Operating result	€ million	2,296	2,506	-8.4
Return on Capital Employed (ROCE)	%	11.0	11.7[1]	-
Weighted average cost of capital (WACC) before tax	%	9.0	9.0	-
Value added	€ million	420	586[1]	-28.3
Capital employed	€ million	20,844	21,327[1]	-2.3
Capital expenditure	€ million	1,203	1,461	-17.7
Property, plant and equipment	€ million	1,147	1,174	-2.3
Financial assets	€ million	56	287	-80.5
		12/31/07	12/31/06	
Workforce[2]		28,472	28,418	0.2

1 Figures adjusted; see commentary on pages 73 and 208 et seq.
2 Converted to full-time positions.

1.6 Key figures by division at a glance

RWE npower		2007	2006	+/– in %
External revenue	€ million	8,920	8,485	5,1
Intra-group revenue	€ million	5	8	-37.5
Total revenue	€ million	8,925	8,493	5.1
EBITDA	€ million	870	658	32.2
Operating result	€ million	724	512	41.4
Return on Capital Employed (ROCE)	%	11.3	7.7[1]	-
Weighted average cost of capital (WACC) before tax	%	10.0	10.0	-
Value added	€ million	82	-153[1]	153.6
Capital employed	€ million	6,424	6,643[1]	-3.3
Capital expenditure	€ million	587	407	44.2
Property, plant and equipment	€ million	587	396	48.2
Financial assets	€ million	-	11	-
		12/31/07	12/31/06	
Workforce[2]		11,975	11,624	3.0

1 Figures adjusted; see commentary on pages 73 and 208 et seq.
2 Converted to full-time positions.

1.7 Financial position and net worth

Central financing. At RWE, Group financing is handled by the corporate headquarters, RWE AG. Only in specific cases do our subsidiaries raise capital directly, e.g. if it is economically advantageous to make use of local credit and capital markets. Furthermore, RWE AG acts as coordinator when Group companies assume a liability by issuing warranties or signing letters of comfort. Pooling these activities is a basic prerequisite for managing and monitoring risks centrally. Moreover, this strengthens our position when negotiating with banks and other market participants.

Financial flexibility. We have flexible financing tools besides our high and stable cash flows from operating activities. We can raise long-term funds on the capital market via a €20 billion debt issuance programme. A US$5 billion commercial paper programme is at our disposal to meet short-term financing needs on the money market and we have a €4 billion syndicated credit line, which serves as a liquidity reserve. At the end of 2007, drawings on the debt issuance programme totalled €11.1 billion. As of December 31, 2007, we had full access to both the commercial paper programme and the syndicated credit line. Half of this credit line has a term of 364 days, and the other half has a term of five years. None of our finance programmes or our credit facility contain specific financial covenants such as interest coverage, leverage or capitalization ratios that could trigger actions, such as acceleration of repayment or additional collateral. Likewise, they do not contain rating triggers.

Credit rating remains high. Creditworthiness assessments by independent rating agencies have a substantial influence on a company's options to raise capital. The better the rating, the easier it is to gain access to international credit markets and the better the conditions for debt financing. Therefore, we benefit from the fact that the two leading rating agencies, Moody's and Standard & Poor's, have both given us the fifth-best credit rating grade (A1 and A+) since the end of 2002. Both of the rating agencies confirmed their ratings in 2007—Moody's in July and Standard & Poor's in November. The following table provides an overview of our credit ratings at the end of January 2008.

Credit rating	Moody's	Standard & Poor's
Long-term	A1 / stable outlook	A+ / negative outlook
Short-term	P-1	A-1

In 2007, our interest expenses (including those for hedges)amounted to 5.8% of the RWE Group's average financial liabilities and were thus higher than in the previous year (5.1%). There are several reasons for this. In sum, there was a rise in interest rates for debt in euros, US dollars and sterling. We have financial liabilities in all these currencies. In addition, there was an increase in the share of debt accounted for by non-current liabilities, which had higher interest rates. Moreover, since we bought back RWE bonds on the market in 2007, we incurred costs mainly amounting to the difference between the fair value and the carrying amount of these securities. We classify these costs as an interest expense.

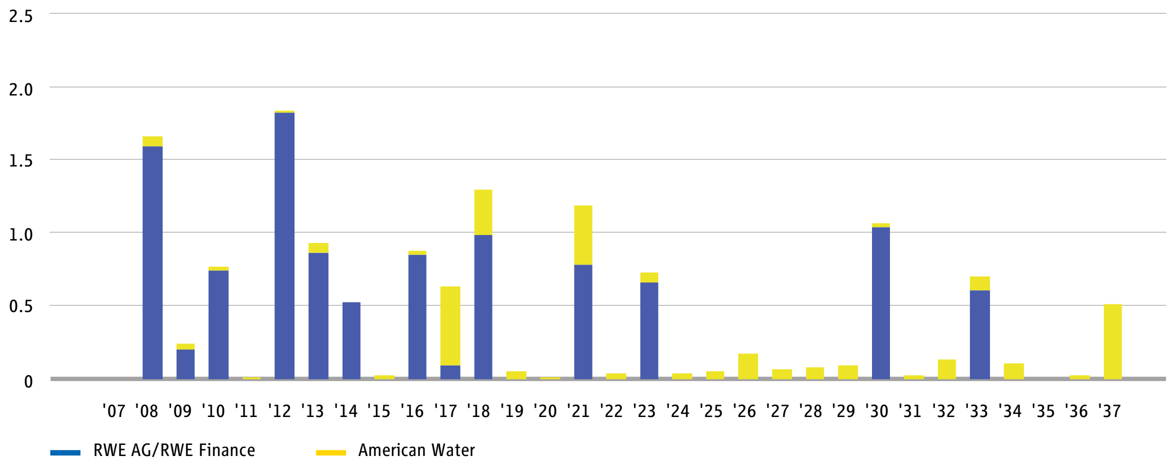
Net debt down to €5.1 billion despite high dividend. As of December 31, 2007, our net debt (net financial assets minus provisions for pensions) amounted to €5.1 billion. The water business, which is stated as a discontinued operation, is still included in this figure. Despite the large dividend payment (€2.2 billion), net debt decreased by €1.8 billion compared with the previous year. This was primarily due to the high level of free cash flow of €2.0 billion. €1.7 billion in capital gains on divestments and fluctuations in foreign exchange rates contributed to the decrease in liabilities. The transfer of €7.9 billion in funds to RWE Pensionstreuhand e.V. reduced net financial assets and—by nearly the same order—provisions for pensions. Therefore, it did not influence net debt.

Net debt € million	12/31/07	12/31/06	+/– in %
Cash and cash equivalents	1,922	2,794	-31.2
Marketable securities	11,302	17,835	-36.6
Other financial assets	2,125	3,473	-38.8
Financial assets of continuing operations	**15,349**	**24,102**	**-36.3**
Bonds, notes payable, bank debt, commercial paper	12,005	18,308	-34.4
Other financial liabilities	1,280	1,074	19.2
Financial liabilities	**13,285**	**19,382**	**-31.5**
Net financial assets of continuing operations	**2,064**	**4,720**	**-56.3**
Provisions for pensions and similar obligations	3,496	11,584	-69.8
Net debt of continuing operations	**1,432**	**6,864**	**-79.1**
Net debt of discontinued operations	3,624	-	**-**
Net debt of the RWE Group	**5,056**	**6,864**	**-26.3**

Nominal volume of RWE bonds outstanding drops to €14 billion. The nominal volume of bonds issued by RWE companies amounted to €14 billion at the end of 2007. The decline compared to the end of 2006 (€16.7 billion) is primarily due to the redemption and buyback of bonds. These were predominantly bonds with nominal amounts totalling €2.2 billion. €1.6 billion in bonds come due in the 2008 financial year. At the end of 2007, the weighted average remaining maturity of bonds issued by the RWE Group was ten years.

American Water issues US$ bonds with a nominal volume of US$2.1 billion. In preparation for the planned initial public offering, American Water repaid intragroup liabilities. In turn, the company placed US$2.1 billion in bonds in the year under review. Most of the bonds were issued by the financing company American Water Capital Corp. and have terms of between seven and 30 years. This removed American Water from the Group's central financing and further strengthened the water utility's independence on the capital market.

Maturity profile of the RWE Group's capital market debt in € billion



RWE Group's capital market debt by remaining term to maturity		0–3 years	4–7 years	8–12 years	> 12 years
Nominal volume	€ billion	1.9	3.5	3.4	5.2
Relative share of total volume of capital market debt	in %	14	25	24	37
Cumulative share of total volume of capital market debt	in %	14	39	63	100

Share of foreign-currency financial debt increased. In 2007, the portion of the RWE Group's financial debt denominated in foreign currency increased due to the redemption of euro bonds and the issuance of US dollar bonds by American Water. Including currency hedges, our debt at the end of 2007 breaks down as follows: 44% in US dollars, 37% in sterling, and 19% in euros and other currencies. The share of debt denominated in euros thus declined by five percentage points compared with the previous year. In 2007, our financial liabilities decreased by €6.1 billion to €13.3 billion.

Cash flow statement € million	2007	2006	+/– in %
Cash flows from operating activities	6,085	6,783	-10.3
Impact of the change in working capital	-222	-534	58.4
Cash flows from investing activities	-4,483	-2,471	-81.4
Cash flows from financing activities	-2,458	-2,948	16.6
Effects of changes in foreign exchange rates and other changes in value on cash and cash equivalents	-16	-1	-
Total net changes in cash and cash equivalents	-872	1,363	-164.0
Cash flows from operating activities	6,085	6,783	-10.3
Minus capital expenditure on property, plant and equipment and in intangible assets	-4,065	-4,494	9.5
Free cash flow	**2,020**	**2,289**	**-11.8**

Cash flows from operating activities up 6% year on year, excluding Thames Water. In 2007, cash flows from operating activities amounted to €6,085 million. This represents a decrease of 10% over the previous year. This was because we sold Thames Water at the end of 2006. In consequence, we did not benefit from the water company's cash flows from operating activities in the year under review, which had amounted to €1,050 million in 2006. Excluding Thames Water, cash flows from operating activities posted a year-on-year increase of €352 million, or 6%. Here, we benefited above all from the earnings improvements achieved by the electricity generation and trading businesses. Furthermore, there were positive effects in working capital. Cash flows from investing activities (including cash investments) were €4,483 million higher than proceeds from the disposal of assets and the sale of companies. Cash flows from financing activities were -€2,458 million. This was largely attributable to dividend payments, which totalled €2.2 billion.

Cash flows from operating activities, minus capital expenditure on property, plant and equipment, result in free cash flow, which amounted to €2,020 million. Free cash flow was thus €269 million, or 12%, below the year-earlier level. This was due to the decrease in cash flows from operating activities owing to the sale of Thames Water in 2006. The decline in capital expenditure on property, plant and equipment was unable to offset this.

Balance sheet structure: equity ratio improved to 17.8%. The development of our consolidated balance sheet was marked by the continued reduction in debt and the transfer of assets via a contractual trust arrangement. These two transactions contributed to the significant decrease in the balance sheet total. As of December 31, 2007, it amounted to €83.6 billion and was therefore €9.8 billion lower than at the end of 2006. As already explained on page 58, we transferred €7.9 billion in assets to RWE Pensionstreuhand e.V. and offset them against the provision for pensions in compliance with IAS 19. These were largely marketable securities held as financial assets (€3.7 billion) and current marketable securities (€4.2 billion). Moreover, we further strengthened our robust financial and capital structure by reducing capital market debt. Long-term capital market debt declined by €5.5 billion and short-term capital market debt was reduced by €0.8 billion. The decline of the US dollar and sterling compared to the euro contributed to the decrease in the balance sheet total. Changes in foreign exchange rates had a total effect of -€1.9 billion.

Balance sheet structure	12/31/07		12/31/06	
	€ million	in %	€ million	in %
Assets				
Non-current assets	41,580	49.7	51,999	55.6
Intangible assets	11,882	14.2	14,901	15.9
Property, plant and equipment	20,038	24.0	26,034	27.9
Current assets	42,051	50.3	41,456	44.4
Securities	10,858	13.0	16,788	18.0
Assets held for sale	8,610	10.3	-	-
Total	**83,631**	**100.0**	**93,455**	**100.0**
Equity and liabilities				
Equity	14,918	17.8	14,111	15.1
Non-current liabilities	36,770	44.0	52,402	56.1
Provisions	21,212	25.4	28,632	30.6
Financial liabilities	10,046	12.0	15,672	16.8
Current liabilities	31,943	38.2	26,942	28.8
Liabilities held for sale	5,875	7.0	-	-
Total	**83,631**	**100.0**	**93,455**	**100.0**

As explained on page 60, we stated American Water, which is for sale, under “Discontinued operations” in the 2007 financial statements. This led to adjustments on the balance sheet: €8.6 billion in current assets were classified as “Assets held for sale.” This is contrasted by €5.9 billion in “Liabilities held for sale” and €2.7 billion in “Equity of operations held for sale” on the equity and liabilities side.

As of December 31, 2007, equity covered 35.9% of our non-current assets. This is much more than in the previous year (27.1%). The equity ratio also rose. At the balance sheet date, it was 17.8% (previous year: 15.1%).

1.8 Notes to the financial statements of RWE AG (holding company)

RWE AG is the management holding company of the RWE Group. It handles general management tasks such as the corporate strategy, corporate finance and corporate accounting. RWE AG's situation is largely determined by the Group's activities.

The financial statements of RWE AG, which have been issued an unqualified audit opinion by PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, are submitted to Bundesanzeiger Verlagsgesellschaft mbH, Cologne, Germany, the operator of the electronic Federal Gazette (Bundesanzeiger) and published in the electronic Bundesanzeiger. They can be ordered from RWE AG and are also available on the Internet.

Financial statements. The financial statements of RWE AG are prepared in accordance with the German Commercial Code and the German Stock Corporation Act. A brief overview is provided below:

Balance sheet of RWE AG (abridged) € million	12/31/07	12/31/06
Non-current assets		
Financial assets	29,546	32,899
Current assets		
Accounts receivable from affiliated companies	5,542	7,134
Other accounts receivable and other assets	925	861
Marketable securities and cash and cash equivalents	4,779	8,540
Total assets	**40,792**	**49,434**
Equity	8,400	7,424
Provisions	6,988	10,468
Accounts payable to affiliated companies	23,515	28,563
Other liabilities	1,889	2,979
Total equity and liabilities	**40,792**	**49,434**

Income statement of RWE AG (abridged) € million	2007	2006
Net income from financial assets	4,130	4,279
Net interest	-1,210	-1,457
Other income and expenses	802	-172
Profit from ordinary activities	**3,722**	**2,650**
Taxes on income	-777	-237
Net profit	**2,945**	**2,413**
Transfer to retained earnings	-1,173	-445
Distributable profit	**1,772**	**1,968**

Assets. The net worth of RWE AG is determined by the management of investments and the activities it undertakes for the Group companies. The holding company holds the shares in the operating companies and handles financing for them. This is reflected in corresponding accounts receivable from and payable to affiliates. At the end of March 2007, €7.9 billion in assets were transferred to RWE Pensionstreuhand e.V. via a contractual trust arrangement (CTA). This only has an impact on the IFRS consolidated financial statements since commercial ownership remains with RWE AG due to the fiduciary relationship. In contrast, the transfer of pension obligations to RWE Pensionsfonds AG in return for €4.6 billion in redemption capital reduced assets and provisions. Provisions for pensions also include coverage for the vested benefits of subsidiaries' current and former employees. RWE AG is reimbursed for pension expenses by the companies concerned. This resulted in a corresponding reduction in income from investments.

As of December 31, 2007, RWE AG's equity ratio was 20.6%, as compared to 15.0% in the previous year. This rise is a result of the reduction in the balance-sheet total and the €1,173 million which were transferred to retained earnings.

Financial position. RWE AG's financial situation is determined by the procurement of funds for its subsidiaries' ongoing business activities. A total of €5.9 billion in external and internal financial debt was repaid in the fiscal year. As a well-known bond issuer on the capital market, RWE AG has launched a €20 billion debt issuance programme. €11.1 billion of the volume had been subscribed by December 31, 2007. The US$5 billion commercial paper programme launched in addition was fully available at the cut-off date.

Earnings position. RWE AG's earnings are largely determined by the earnings generated by its subsidiaries. Net income rose by 22% to €2,945 million. This was due to the marked improvement in earnings posted by major subsidiaries. Therefore, there was also a significant rise in income taxes paid by these companies, which we recognize under "Other income and expenses." Income from financial assets was slightly down year on year. It largely consists of earnings contributed by RWE Power AG and RWE Energy AG. These were affected by one-off effects connected to the measurement of investments and the initial funding of the RWE Pensionsfonds, which had an effect on costs. In the previous year, income from financial assets still reflected the one-off effects of the sale of Thames Water as well as the negative impact of the measurement of provisions for pensions. Net interest improved compared to 2006, because the sale of Thames Water caused financial debt to decrease. RWE AG's tax expense increased; the capitalization of the non-interest-bearing corporate tax credit due to new tax laws had resulted in a positive one-off effect in the previous year.

The Supervisory and Executive Boards of RWE AG will propose to the Annual General Meeting on April 17, 2008, that a dividend of €3.15 per share be paid for fiscal 2007. Relative to the Group's recurrent net income, this results in a payout ratio of 60%. We are thus at the upper end of the target range of 50% to 60% envisioned for the 2007 financial year.

Disclosure of takeover provisions: disclosure in compliance with Secs. 315, Para. 4 and 289, Para. 4 of the German Commercial Code (HGB) and report of the Executive Board in accordance with Sec. 120, Para. 3, Sentence 2 and Sec. 175, Para. 2, Sentence 1 of the German Stock Corporation Act (AktG). RWE AG's subscribed capital remained unchanged, consisting of 523,405,000 no-par-value common shares in the name of the bearer (93.1% of the subscribed capital) and 39,000,000 no-par-value preferred shares in the name of the bearer without voting rights (6.9% of the subscribed capital). The remaining rights and obligations are determined by the German Stock Corporation Act. Holders of non-voting preferred shares have a right to a preferred share of profits of €0.13 per share when the distributable profit is distributed. The composition of subscribed capital and—above all—the legal definition of the non-voting preferred shares issued by RWE are in compliance with the provisions of the law and of the Articles of Incorporation.

In compliance with Sec. 21, Para. 1 of the German Securities Trading Act (WpHG), on December 21, 2007, RW Energie-Beteiligungsgesellschaft mbH & Co. KG, Dortmund, informed us that it held 16.089% of RWE Aktiengesellschaft's voting stock at the time.

Executive Board members are appointed and dismissed in accordance with Secs. 84 et seq. of the German Stock Corporation Act (AktG) in connection with Sec. 31 of the German Co-Determination Act (MitbestG). Amendments to the Articles of Incorporation are made pursuant to Secs. 179 et seqq. in connection with Sec. 16, Para. 5 of the Articles of Incorporation of RWE Aktiengesellschaft. According to Sec. 16, Para. 5 of the Articles of Incorporation, unless otherwise provided for by law or in the Articles of Incorporation, the General Meeting shall adopt all resolutions with a simple majority of the votes cast; in as far as a majority of the capital stock represented is furthermore required for resolutions to be adopted, the simple majority of the capital stock represented shall suffice. RWE's Articles of Incorporation have thus made use of the legal possibility of determining a different capital majority for amendments to the Articles of Incorporation than prescribed by law. Amendments to the Articles of Incorporation that only concern the wording, i.e., only make linguistic changes, without changing content, may be decided upon by the Supervisory Board (Sec. 10, Para. 9 of the Articles of Incorporation).

Pursuant to the resolution passed by the Annual General Meeting on April 18, 2007, the Executive Board was authorized to purchase shares of any class in RWE until October 17, 2008, totalling up to 10% of the share capital. It is at the Executive Board's discretion to purchase the shares on the stock market or by making a public call for shares. They may then be called in, transferred to third parties within the scope of mergers or acquisitions, or sold in another manner. The authorization may be exercised in part or in full.

RWE AG's syndicated credit line has a change of control clause in line with generally accepted practice. It is a contractual provision which grants a contracting party certain rights (most importantly the right to termination) in the event of a change of control or the majority shareholder at the other contracting party.

The 2005 long-term incentive plan (Beat) for the Executive Board and executives of RWE AG and of affiliated companies includes a provision for a change of control. In such events, all holders of performance shares under the Beat programme receive a compensatory payment. The amount of the compensatory payment is determined by multiplying the price paid for RWE shares as part of the takeover by the final number of performance shares. The latter is determined when the takeover offer is made, in line with the plan conditions. Before the last amendment made to the German Corporate Governance Code, the President and CEO, Dr. Jürgen Großmann, was granted a special right of termination in the event of a change of control. On exercise of the special right of termination, Dr. Jürgen Großmann receives a one-time payment that covers the remuneration due him until the end of the agreed contractual period, including a contractually agreed amount of pension capital.

The authorization to conduct share buybacks, the provision governing changes of control over the syndicated credit line and the compensation regulations for the 2005 long-term incentive plan (Beat) that prescribe compensation for performance shares in the event of a change of control, are in line with the generally accepted standards of German capital market-oriented companies.

1.9 Innovation

Research and development: focus on climate-friendly and more efficient power plants.

The energy sector is in need of innovation. Secure, affordable and climate-friendly power supplies will be impossible without technological progress. Therefore, RWE is stepping up its research and development. We will significantly increase spending in this field in the years ahead. We want to pave the way for a new method of generating electricity from coal, involving the capture of carbon dioxide emissions and their storage under ground.

Efficiency improvements and emissions reductions in fossil fuel-fired power plants are the main focus of research and development (R&D) measures within the RWE Group. In this field, we co-operate with partners in the plant engineering and chemical industries. Therefore, these R&D activities are only partially included in our R&D spending. In the year under review, we spent €74 million on research and development, which was slightly higher than the level achieved in 2006 (€73 million). In addition, we capitalized €52 million in development expenditure (previous year: €62 million). We entrusted a total of 270 staff members with R&D tasks. We will step up our R&D work considerably, causing expenditure in this area to grow significantly.

One of the main determinants of our competitiveness is whether we succeed in bringing the generation of electricity using fossil fuels—especially coal—in line with climate-protection goals. Among the keys to achieving this is the capture and storage of carbon dioxide produced during the electricity generation process. We are currently preparing to construct the world's first large-scale coal-fired power plant using this type of technology. This involves combining coal gasification with carbon capture and generating electricity using turbines located downstream of these processes. This is referred to as IGCC (integrated gasification combined cycle) technology. This process gives one the option of manufacturing products gas such as synthetic natural gas, hydrogen and fuel from the coal gas, instead of electricity. The planned IGCC plant is scheduled to go online in 2014.

In addition to IGCC, the separation of carbon dioxide from flue gas ("CO_2 scrubbing") enables the generation of electricity from coal in a climate-friendly manner. The advantage offered by CO_2 scrubbing is that it can be implemented in existing power plants by retrofitting them with appropriate units. In 2007, RWE Power joined forces with BASF and Linde to refine this technology. The joint project envisions the construction and operation of a pilot in our lignite-fired power station in Niederaussem, Germany, which we intend to commission in the middle of 2009. The purpose of the pilot is to examine new CO_2 scrubbing solutions. Furthermore, the capture processes will be tested under real-life conditions and readied for large-scale use. Our goal is to commercialize carbon capture in lignite-fired power plants by 2020. We will then be able to remove more than 90% of the carbon dioxide from the waste gases produced during combustion and then store it under ground. On completion of the pilot tests, a decision on a demonstration plant will be taken in 2010.

We want to make inroads with CO_2 scrubbing in hard coal power stations as well. This is a field in which RWE npower has assumed a pioneering role. Our UK subsidiary will build a 1-MW pilot facility in its coal-fired power plant in Aberthaw, UK. Furthermore, construction of a 25-MW demonstration unit is planned for Tilbury, UK. Another ground-breaking project has been launched by RWE Power. The subject of the research work is an ammonium-based separation method that was developed by Alstom. RWE Power and the US utility American Electric Power (AEP) have agreed to test this technique in AEP's Mountaineer hard coal power station (1,300 MW) in New Haven, West Virginia, USA. Altogether, the RWE Group has set aside a budget of €93 million for projects related to CO_2 scrubbing.

If the low-CO_2 power plant concept is to become reality, we must find a way to store carbon dioxide. We are conducting our own projects and participating in research consortia to examine the possibility of safely storing CO_2 in former gas storage facilities and in deep geological formations. At present, we are running an initial round of tests in the vicinity of Ketzin, Brandenburg, Germany. This is where a total of 60,000 metric tons of CO_2 will be stored in a deep layer of sandstone. This will be done between 2008 and 2010 as part of the EU's CO2SINK research project. We hope to obtain knowledge on the dispersion behaviour of carbon dioxide.

By taking the aforementioned measures, we want to play our part in ensuring that hard coal and lignite can continue to help cover energy demand despite increasingly strict climate-protection standards. However, policymakers will need to play their part, too. Most importantly, a binding legal and regulatory environment that provides us with the planning security necessary to store CO_2 in geological formations must be created on national and European levels.

The capture and storage of CO_2 inevitably leads to losses in efficiency. This is why it is all the more important to continue work on improving the efficiency of our power plants. One highlight in this context is the construction of a demonstration plant in which lignite will be pre-dried before combustion at our site in Niederaussem, Germany. This is scheduled for commissioning in 2008. Fluidized-bed drying with integrated heat usage, the method being applied here, was engineered and patented by RWE. We have already issued a license to a third party. With this technology, lignite-based power production can gain four percentage points in terms of efficiency.

Efficiency improvements of a similar order can be achieved by using what is termed a 700-degree power plant. The new 'Component Test Facility for a 700°C Power Plant' (COMTES700) situated in the Scholven hard coal-fired power station in Gelsenkirchen, Germany, will help to reach this goal. Together with partners in Germany and abroad, our engineers are putting next-generation materials and power plant components to the test in COMTES700. These components provide reliable performance under high pressure and at temperatures exceeding 700 degrees centigrade. The project is subsidized by the European Union. Results are expected to be presented in 2009. After that, the researchers and engineers will be faced with the next challenge: the construction of a demonstration power plant to provide conclusive evidence of the technology's commercial readiness. In the medium term, the aforementioned projects—lignite pre-drying and the 700-degree power plant—will make it possible to generate electricity from coal with efficiencies of more than 50%. The European average is currently much lower, at 36%.

We are intensifying our research and development work in the field of renewable energy as well. One priority is to find new ways to use biogas to generate both electricity and heat. RWE Innogy has joined forces with the University of Bochum, Germany, to explore the use of corn (maize) silage for the production of biogas and ways to increase gas yield in a 700 kW pilot power plant. Furthermore, we have already started to do preparatory work for a project processing biogas to natural gas-quality biogas. This could then be fed into the gas grid. Another priority is investigating methods to improve the output of wind power stations and optimally integrate them into the power grid. For this purpose, we are concentrating on improving wind prediction and plant reliability. In this context, the construction, connection and operation of offshore wind farms constitute a huge challenge.

RWE Innogy also invests in technologies suitable for generating electricity from the movement of water caused by tides and waves. We are closely cooperating with a leading plant supplier to obtain a permit for the first commercial ocean/tidal flow turbine demonstration project. This will be located off the coast of Anglesey, Wales, with an installed capacity of 10.5 MW. We are also planning a 4-MW wave power plant off the Isle of Lewis in the Scottish Hebrides. Forty generators along a 250 metre-long breakwater-type structure will generate electricity from the surf. In addition, RWE Innogy is carrying out several demonstration projects exploring the use of geothermal energy.

An integral component of RWE Innogy's business model is investment in emerging technology companies, particularly financing companies going through their startup and growth phases. We are thus providing major stimuli for forward-looking technologies in Germany and Europe.

In many respects, power utilities face new challenges in the expansion of renewable generation capacity. The volume of electricity that can be fed into the grid will fluctuate significantly. Therefore, it is important to develop new, efficient storage concepts early on. Against this backdrop, RWE Power concluded an agreement with General Electric (GE) in December 2007 to engineer a pressurized-air storage power station. Phase one of the project will involve a feasibility study, which will serve as a basis for a development programme. Phase two envisions the construction of a demonstration plant. When electricity supply is high, pressurized-air storage power plants compress air and force it into subterranean caverns where it is stored. This compressed air can be used to generate electricity when needed. A major challenge for this project lies in the development of suitable components, above all in the field of compressor and heat storage technology, which are necessary in order to ensure high efficiency in pressurized-air storage power plants.

Nuclear energy is another field in which we do R&D work. Accounting for about 25% of Germany's power production, it is clearly the most important source of CO_2-free electricity generation. To ensure that our nuclear power stations are run safely and profitably, we upgrade them to the state of the art continuously. Our R&D activities in this field pursue the same goal. This is an area in which we cooperate with the European association for power and heat generation, VGB PowerTech e.V. Another item on the agenda is the development of reactors that are optimized in terms of both safety technology and economic viability. By taking these steps, we want to keep the door open for the use of nuclear energy against the backdrop of an ever-changing energy industry and societal environment. Seeking to secure and amass know-how in the field of nuclear energy in Germany, we are supporting nuclear research and teaching at the technical university in Aachen by funding a foundation professorship.

We have stepped up our R&D work in the upstream sector. It aims to maintain the already high success rate of our exploration drilling. We are looking into ways to improve the quality of the assessments we make of indications of hydrocarbon deposits. To this end, we are conducting extensive geological studies in North Africa. We are also looking into the possibility of obtaining clearer graphical representations of deposit structures in order to be able to interpret them more accurately. Another item on the R&D agenda was efficiency improvements in production.

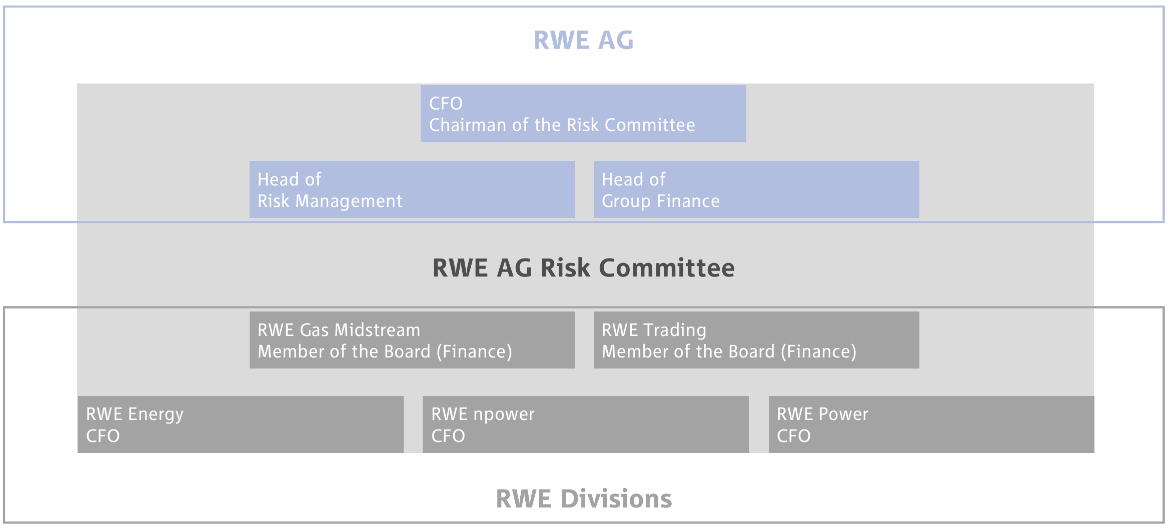
Methane obtained from gas hydrates has great potential to become an energy source of the future. Gas hydrates are formed when natural gas blends with water to form an icy mass. There are large gas hydrate reserves in permafrost regions and on the ocean floor. Finding ways to make use of them is the objective behind two of RWE Dea's research endeavours. One of them opens the door to entirely new prospects in terms of climate protection: It explores ways to implement CO_2-free methane recovery while storing carbon dioxide as a hydrate.

Our R&D operations are also dedicated to the safe, economical and environmentally-compatible operation of our electricity and gas grids. Last financial year, we successfully concluded a large number of projects in this field. Among other things, we tested a system for identifying faulty cables in the local grid both affordably and without causing interruptions of service. In the future, this method will be standard procedure at RWE. Furthermore, we want to break new ground in the measurement of power consumption. At present, we are testing automatic meter reading. This term designates a new generation of electricity meters that enable households to track their consumption at any time. This will give customers better control of their electricity usage, stimulating thriftier consumption. Another advantage of this technology is that bills can be prepared without the need for on-site meter readings.

1.10 Development of opportunities and risks

Risk management: organizational structure. The RWE Group has a groupwide risk-management system for the early identification as well as standardized reporting, assessment, control and monitoring of risks. We have formed risk-management boards both at the Group and divisional levels. They are responsible for the risk management system's continued development and establish rules for the risk-management process. The basis for this is provided by a groupwide risk management guideline.

In addition, the Executive Board of RWE AG has entrusted a Risk Committee with the management of risks arising from the volatility of the price of commodities and of credit risks arising from trading, sales and procurement activity. This committee meets on a monthly basis. This ensures that the risks that are most important to us are closely monitored. As Chairman of the Risk Committee, the CFO of RWE AG is responsible for planning, managing and monitoring the aforementioned risks. The Head of Risk Management and the Head of Group Finance of RWE AG support him in making decisions. In 2007, the CFOs of RWE Power, RWE Energy and RWE npower as well as the managing directors of RWE Trading and RWE Gas Midstream responsible for risk controlling and finance also sat on the Risk Committee. They saw to it that the Risk Committee's guidelines are implemented uniformly across their organizational units. The Risk Committee will be adapted to our new organizational structure. We will decide on the Committee's exact composition over the course of 2008.



Risk-management process. Our risk-management activities are designed to obtain information on risks and their financial impact as early as possible, in order to be able to counteract them with suitable measures. Moreover, the planning and controlling process also aims to identify opportunities and make use of associated earning potential. We evaluate risks according to their probability of occurrence and damage potential and aggregate them at the business unit, divisional and Group levels. The damage potential is defined against the operating result and equity of the business unit concerned and the Group as a whole. We can thus ensure a systematic and uniform analysis of our current risk situation throughout the Group, on the basis of which specific risk-control initiatives can be developed. Our risk reporting scheme is fully integrated in our standardized planning and controlling process. The RWE Group's management and supervisory bodies are regularly informed of the current risk situation. The efficiency and effectiveness of our risk management system is monitored internally.

Opportunity and risk categories. We break down major risks and opportunities into the following categories:

- ***The future of the company:*** At present, there are no identifiable risks that could jeopardize the continued operation of RWE AG or the RWE Group.

- ***Changes in the general economic climate:*** Economic trends in our core markets can affect the degree of capacity utilization, having either a positive or negative impact on results.

- ***Volatility of commodity and product prices:*** Risks and opportunities arise for the RWE Group above all in our electricity generation business. The latter is significantly influenced by the development of market prices for electricity, fossil fuels—especially hard coal and gas—as well as by the development of the price of CO_2 certificates. A risk arises, e.g., if higher commodity prices cannot be passed on by increasing electricity prices. Opportunities stem from the higher margin between electricity prices and prices for fossil fuels. Additional risks and opportunities stem from our oil and gas production operations. The impact of unexpected disadvantageous changes in price in this area is minimized through the strategic use of derivative hedges. In addition to production, supply operations are also exposed to risks. Such risks arise, e.g., as a result of unexpected fluctuations in demand owing to changes in temperature. Our price risks on purchasing and sales markets are determined using special evaluation models, while taking current forward prices and expected price volatility into account. Among other things, we use financial and commodity derivatives to mitigate risks associated with sales and procurement.

Our electricity and gas businesses face price and sales risks as well as marketing opportunities resulting from the deregulation of Europe's electricity and gas markets. We address these risks with differentiated pricing strategies and appropriate marketing policies as well as with effective measures to cut costs. Earnings risks can also arise from the loss of concessions in the grid business.

We limit earnings risks stemming from price fluctuations on energy markets for the generation and sales businesses through our energy trading activities. Furthermore, we intend to generate profits by taking trading positions. On the one hand, in this context, our trading business functions as a central platform for hedging commodity price risks throughout the RWE Group. This enables us to create a stable basis of planning for our company. On the other hand, while staying within trading limits, we conclude trades in order to take targeted advantage of changes in prices on the energy markets. This leads to risks from unexpected price fluctuations. In addition, we are also exposed to credit risks in the event that counterparties fail to fulfil their contractual obligations. The RWE Group's integrated trading and risk management system for the energy trading business is firmly aligned with best practice as applied to the trading business. Specific benchmarks for price risks are established on a daily basis. The RWE AG Risk Committee sets risk limits that are continuously monitored. Among other things, we calculate the Value at Risk (VaR) to quantify price risks associated with energy trading. A system of limits established by RWE AG's Risk Committee limits the respective risks. The central risk controlling parameter is the Global Value at Risk, which has a cap of €40 million and applies to all of the trading transactions concluded by RWE Trading. The VaR figures within the RWE Group are generally based on a confidence interval of 95% and a holding period of one day. The Global VaR thus indicates the maximum daily loss from all trading transactions, which RWE Trading does not exceed with a probability of 95%. At the end of 2007, the Global VaR used by RWE Trading amounted to €10 million. In the period under review, it averaged €15 million.

- ***Volatility of financial prices:*** Within the scope of our operations, we are also exposed to currency, interest-rate and share-price risks. Due to our international presence, currency risk management is very important. Sterling and US dollar are our major foreign currencies: We conduct commercial transactions in both these currency zones. Furthermore, fuel prices are quoted in these currencies. Group companies are generally obliged to hedge all currency risks via RWE AG. The parent company determines the net financial position for each currency and hedges it with external market partners if necessary. The Value at Risk is used to measure risk. At the end of 2007, the VaR for RWE AG's foreign currency position was less than €1 million.

Interest rate management is also ascribed significant importance. Our interest-rate risks primarily stem from our financial debt and interest-bearing investments. Negative changes in value caused by unexpected interest rate movements are hedged with non-derivative and derivative financial transactions. On December 31, 2007, the VaR for the interest-rate risk associated with our financial debt and related hedges was €69 million. The VaR from interest-bearing investments including hedges amounted to €21 million. We are also exposed to both risks and opportunities associated with share investments. At the end of 2007, the VaR for share-price risks was €17 million.

Opportunities and risks from changes in the value of securities are controlled by a professional fund management system. The Group's financial transactions are recorded using centralized risk management software and monitored by RWE AG. This enables the balancing of risks across individual companies. Range of action, responsibilities and controls are set forth in internal guidelines to which our Group companies are obliged to adhere.

- ***Creditworthiness of business partners:*** Most of the credit transactions performed by our finance and trading departments are with banks and business partners of good creditworthiness. We mitigate credit risks from these activities by placing limits on transactions and— if necessary—receiving cash collateral. In addition, we conclude credit insurance policies and bank guarantees. Credit risks are monitored daily for energy trading transactions and weekly for finance transactions. In our supply business, we are exposed to credit risks due to the possibility that customers may fail to meet their financial obligations. We mitigate this risk by subjecting our customer portfolio to regular creditworthiness checks on the basis of credit risk guidelines.

- ***Liquidity:*** Liquidity risks arise if liquidity reserves are no longer sufficient for the Group to meet its financial obligations in a timely manner. Such obligations result from the refinancing of the liabilities. Furthermore, we are obliged to put up cash collateral within the scope of our trading transactions with counterparties, in order to collateralize negative market values. Cash and cash equivalents and current marketable securities worth a combined €12.8 billion (as of December 31, 2007) are available to cover the resulting liquidity requirement. In addition, we have a considerable amount of unused funds from the aforementioned US$5.0 billion commercial paper programme, €20.0 billion debt issuance programme as well as a fully committed syndicated credit line of €4.0 billion. This makes the liquidity risk very low.

- ***Continuity of business activities:*** We operate technologically complex and interconnected production plants all along our value chain. Earnings risks can arise from uninsured damage to our lignite mining equipment, production plants, power plant components and grids. There is an increasing risk of outages in our power plants due to the ageing of their components. Furthermore, new power plants being built may experience delays due to unforeseen events, e.g., accidents or property damage. Our grid business is exposed to the risk of facilities being destroyed by force majeure such as severe weather conditions. We address these risks through high safety standards as well as regular audit, maintenance and servicing work. As appropriate, insurance policies also limit possible effects of damage.

- ***Regulation:*** The RWE Group's exposure to the constant change in the political, legal and social environment in which it does business can be expected to have an impact on earnings. Lignite and hard coal power plants account for a significant portion of our electricity generation portfolio. This represents a risk due to the EU-wide CO_2 emissions trading system. Risks can arise from unexpected increases in the price and the associated rise in the cost of procuring CO_2 certificates. Therefore, CO_2 price risk management is an integral component of our centralized risk-management system. The European Commission adopted a new set of climate-protection measures for the period from 2013 to 2020. They include binding goals for all EU member states regarding the reduction of greenhouse gas emissions and the share of electricity consumption accounted for by renewable energy. But the details of an international or European emissions trading system remain largely unclear. However, RWE anticipates that costs will be much higher than in the current trading period, which will last until 2012. We intend to continue reducing CO_2 emissions and make our power generation portfolio more flexible by investing in power plants in the future. Furthermore, we limit CO_2 risks through climate-protection projects in developing and newly industrializing countries within the scope of the Kyoto "Clean Development Mechanism" (CDM) and "Joint Implementation" (JI).

  Risks exist in our German electricity and gas grid businesses as a result of regulatory intervention, especially against the backdrop of the cost review that is currently being conducted by the regulatory authority. A significant reduction in grid revenue is to be expected. The German Federal Network Agency has issued the first set of notices for the electricity sector. Now there is more clarity as regards incentive-based regulation from 2009 onwards. The regulation's cornerstones have been laid out in a directive which was passed by the German Upper House in September 2007. We intend to partially offset some of the negative effects stemming from the regulation by taking measures to cut costs and enhance efficiencies throughout RWE Energy. We are also exposed to regulatory risks within the scope of our Eastern European activities—above all in the Czech gas business.

In Germany, risks can also arise from the stricter monitoring of anti-competitive pricing practices, which entered into force at the end of 2007. This can increase the number of investigations and legal disputes under antitrust law. To make a more accurate assessment, we will have to wait until the concrete thrust of such procedures becomes apparent.

- ***IT security:*** RWE has established a mandatory groupwide process for engineering, managing and auditing IT projects in order to manage IT risks during the development of IT solutions designed to support business processes. The IT solutions are largely based on standard, commercially available software. IT operations are run in modern computing centres with continuously updated IT infrastructure which is subject to a groupwide security directive.

- ***Capital expenditure and divestments:*** Decisions approving acquisitions and capital expenditure on property, plant and equipment must take into account both the opportunities and risks associated with tying up capital for extensive periods of time. At RWE, such decisions are prepared and implemented in adherence with specific accountability rules and approval processes. The same applies to divestments such as the planned sale of American Water.

- ***Competing for qualified staff:*** We compete with other companies for the best talent in an increasingly contested market. This involves opportunities and risks, especially in light of our ambitious organic earnings growth targets. To secure and strengthen RWE's position when competing for qualified personnel, in our HR management work, we highlight RWE's attractiveness as an employer and strive to retain experts and executives over the long term. In addition to performance-based compensation and progressive employee benefits, we put a lot of effort into the varied prospects offered throughout the RWE Group: trainee programmes, cross-disciplinary career paths, assignments in various European Group companies, and attractive continued education and advanced training offerings.

- ***Legal procedures:*** RWE Group companies are involved in litigations and arbitration proceedings connected with their operations. In addition, out-of-court claims have been filed against individual Group companies in connection with sales of companies. However, we do not expect any major negative repercussions on the RWE Group's economic or financial position. Furthermore, Group companies are directly involved in various procedures with public authorities or are at least affected by their results.

Raw materials production and power generation activities might be curtailed by risks arising from approval processes for our opencast mines and nuclear power plants. Furthermore, there is a risk of financial loss when capital is spent on the construction of power plants in the run-up to local planning decisions made by public authorities. We take precautionary measures against this by preparing our applications for approval with great care and ensuring that approval processes are handled competently. In light of our extensive growth programme and numerous investments in replacement plants, the number of our ongoing approval processes is especially high at present.

Outside shareholders initiated several legal proceedings to examine the appropriateness of the conversion ratios and the amount of cash paid in compensation in connection with company restructurings pursuant to company law. The conversion ratios and cash compensation have been calculated on the basis of expert opinions and verified by auditors. If the legally enforceable decisions come up with a different result, the compensation will be carried out by making an additional cash payment to the affected shareholders, including those who are not involved in the conciliation proceedings.

The EU Commission conducted follow-up inquiries at several European power utilities in May and December of 2006. This also affected RWE Group companies in Germany. Afterwards, the EU Commission filed requests with companies including RWE for information on individual energy market issues.

The EU Commission initiated an abuse procedure against RWE in early May 2007. It suspects that we hindered access to the natural gas transmission system located in Germany in order to attain a purportedly market-dominating position in the gas supply business. This allegation primarily affects RWE Transportnetz Gas, a subsidiary of RWE Energy. However, the Commission expressly points out that the initiation of this procedure does not mean that it has conclusive evidence of any wrongdoing by RWE.

In sum, thanks to its uniform, company-wide risk management practice, the RWE Group is capable of counteracting all aforementioned risks and taking advantage of opportunities as they arise.

1.11 Outlook for 2008

US credit crisis to dampen economic growth. Global economic growth is likely to be weaker in 2008 than in 2007 (3.2%). However, it is unlikely to fall far below 3%. Cyclical risks have become more significant. In the USA, the subprime crisis could push real gross domestic product (GDP) growth down below 2% for the first time since 2002. Experts are of the opinion that a recession is conceivable. The degree to which the US economic crisis will spill over to other industrialized countries cannot be predicted at present. But it is deemed unlikely that GDP growth in the Eurozone will be significantly curtailed. Economists expect that this will also apply to Germany. The German economy's strong international competitiveness should have a stabilizing effect. The momentum of economic growth in the UK is likely to slow more, above all due to weaker income growth and the poorer corporate earnings outlook. The momentum of the economy in EU member states in Central Eastern Europe will remain strong. Some of these economies may expand by more than 5%.

Prices for oil, gas and hard coal to remain high. Despite the slowing world economy, pressure from demand on global energy markets will hardly let up, primarily because of the major need for raw materials in newly industrializing countries such as India and China. This is contrasted by continuing limited production and transportation capacity. At the same time, energy markets are subject to sudden influences stemming, e.g., from weather conditions and political action. The situation on the international oil markets remained tight through January 2008. At the end of the month, a barrel of Brent traded at US$92. Market signals indicate a slight easing. Nevertheless, the price of Brent averaged over the year will probably still be higher than 2007's comparable figure (US$72 per barrel). Since gas supply agreements are still commonly coupled to developments on the oil market and the price formulae have a time lag, our initial prediction is that natural gas will become more expensive in 2008. Should oil prices fall, the effect of the reduction would be felt over the course of the year on the gas market as well. Hard coal prices continue to be at an extremely high level. At the end of January, a metric ton cost US$138 in Rotterdam spot trading (including freight and insurance to Rotterdam). A substantial decline is not foreseeable at present. Therefore, we expect that prices will be at least on par with 2007 levels (US$89) for the full year. The same applies to German BAFA prices.

CO_2 emissions trading: prices for 2008 certificates unlikely to fall. We expect CO_2 emissions allowances to continue to fetch high prices in European trading. As already explained on pages 46 and 50 et seq., the framework conditions have been tightened. Whereas carbon dioxide emissions in Europe could be fully covered by state certificate allocations until 2007, this will cease to be the case going forward. As a result, many major power producers will have to obtain additional certificates. Alternatively, they can curb CO_2 emissions by making less use of high-emissions power plants. Emissions trading will provide the price signals required for this.

CO_2 certificates for 2008 have traded around the 20-euro mark for some months. On January 31, 2008, they traded at €19 per metric ton of CO_2. We believe a significant price decrease is improbable.

High electricity prices across Europe. Electricity prices are also expected to remain high. This is the result of market expectations regarding the development of costs associated with fuel prices and CO_2 certificates. In addition, we anticipate that generation capacity on many European energy markets will continue to be scarce. Recently, electricity prices on the German forward market have stabilized at a high level. Base-load contracts for delivery in 2009 traded at €61 per MWh at the end of January 2007. Prices quoted for electricity in the UK have been on the rise since the middle of 2007. This trend was recently confirmed. At the end of January, the forward price for 2009 base-load deliveries was £51 per MWh (€68 per MWh), which was much higher than the prior-year average. The RWE Group has already sold forward more than 90% of its 2008 electricity production. We have also sold part of our 2009 electricity generation (already more than 40% in Germany).

Strategy Agenda 2012: "More Growth, less CO_2." Today, RWE is one of Europe's most powerful energy groups. In the last few years, we have focussed on the strengths we have nurtured over time—electricity and gas—and have considerably expanded our financial room for manoeuvre. We want to convert this into further added value for our shareholders. On the back of our Strategy Agenda 2012 (see pages 28 and 38 et seqq.) we want to ensure that we remain among the five leading power utilities in Europe going forward. Continued profitable growth is the centrepiece of this strategy. In this regard, we give priority to organic growth. One of the main objectives of our investing activity is to reduce the Group's CO_2 emissions sustainably. More efficient business processes and structures are another important building block.

We set ourselves ambitious operating and financial goals:
- We intend to increase the operating result through organic growth by an average of 5% per year through 2012.
- We want to lift recurrent net income, which is the basis for determining the dividend payment, by an average of 5% to 10% per year through 2012.
- This financial year, we will significantly expand our efficiency-enhancement programme, which will run until the end of 2010. For this purpose, we have begun to subject our key business processes to a comprehensive analysis. So far, we have planned steps to reduce costs and increase revenue that will gradually improve our annual earnings by a total of €600 million.

Capex campaign for profitable organic growth. Investments in infrastructure are key to enabling future growth. The starting shot for the largest capital expenditure programme in RWE's history has been fired. We will lift our former investment budget by almost a third to an average of €6.5 billion per year. In total, we intend to invest more than €30 billion by 2012. Every second euro has been earmarked for projects promoting organic growth. First, we want to cement and maximize the market positions we command on our two largest markets, i.e., Germany and the UK. Centre stage will be taken by new large-scale power plants with which we want to replace old facilities or gain market share. The Netherlands are another point of focus. We will spend significant amounts of capital on our electricity and gas grids as well as on customer service. At the same time, we are making preparations to tap new markets. This will involve the gradual entry into southern Europe's growth regions, including Turkey and Greece. We are also exploring the Russian market. These markets are very attractive for us, because they possess more long-term growth potential than our more mature markets due to their relatively old infrastructure and rising demand for electricity and gas. Furthermore, they offer us the possibility of broadening the geographic spread of operations in our Group. New market opportunities will also open up to us through our entry into the global market for liquefied natural gas and the international large-scale pipeline businesses. We already have positions in these fields, but still lack the critical mass to compete at an international level. In the midstream market, we intend to gradually increase the gas position we have as buyer and seller by a total of 50% to 60 billion m^3 per annum in this sector. The new division, RWE Supply & Trading, which will be created by combining RWE Trading and RWE Gas Midstream, will serve as a platform in this business. This is where we will pool all our non-regulated midstream activities (transmission, storage, procurement and trading) and place them under one roof. We want to double gas production by 2012/13 and thus further reduce our dependency on gas purchasing. In the field of nuclear power, we are pursuing a longer-term growth strategy. This year, we will set the course for power plant new build projects in three Eastern European markets: Bulgaria, Romania and Lithuania. We are participating in the bidding processes for these ventures. In parallel, we are examining a possible entry into future new build projects in the UK.

Substantial increase of renewable energy generation capacity. We intend for wind, hydroelectric and biomass power to feature much more prominently in our future power plant portfolio. This is how we want to take part in the increase in the use of renewables-based energy, while improving our CO_2 balance. In the UK, we are already among the premier electricity producers in this field. Through RWE Innogy, which we founded effective February 1, 2008, we intend to achieve similar prominence on a pan-European level. Our goal is to increase our renewables-based power plant capacity to 4.5 GW by 2012, and we will invest at least €1 billion a year on average to this end. RWE Innogy pools our expertise in this area and has the lean and flexible setup needed to tackle this fragmented market.

Sustainable CO_2 avoidance. EU emissions trading causes the cost of power production to rise considerably. We will rise to this challenge by reducing our CO_2 emissions significantly. All our large-scale capex projects in the field of electricity generation are pursuing this goal. We have identified the potential to avoid more than 20% of our 2006 emissions during the period ending in 2012. We believe that a total of over 30% is conceivable by 2015. The key tools for achieving this are the replacement of existing emissions-intensive power stations, the increase of renewable energy generation capacity, the continued operation of German nuclear power plants, and CO_2 avoidance projects outside our core markets within the scope of the Kyoto "Clean Development Mechanism" (CDM) and "Joint Implementation" (JI) mechanism.

Selective acquisition strategy. Acquisitions are also part of the Strategy Agenda 2012. We constantly examine new projects that afford us the opportunity to enter the aforementioned markets. However, the present wave of consolidation in the European utility sector has driven prices of companies to levels we feel are unacceptable. We join bidding processes only if our profitability criteria are met. Acquisitions must earn their cost of capital no later than the third full year following the date of consolidation.

Changes in reporting structure. In the new fiscal year, we will give our financial reporting a new segment structure. We will present RWE Supply & Trading—formed by combining RWE Trading with RWE Gas Midstream—as an independent division. RWE Trading was previously part of the "Power Generation" Business Unit within the RWE Power Division. We used to report RWE Gas Midstream under "Other, consolidation" as part of the RWE Energy Division. In the future, we will report RWE Dea, a business unit of RWE Power thus far, as an independent division. The reason for this is that the RWE Group's upstream business will display above-average growth. We adjust prior-year figures accordingly. Figures for RWE Innogy, which was launched in February 2008, will initially still be included in "Other, consolidation" at the Group level. Our outlook for the current financial year is already based on the new reporting structure. As in 2007, the Water Division (American Water) will be stated under "Discontinued operations."

Group revenue expected to be higher year on year. Revenue for fiscal 2008 is anticipated to surpass last year's level. This and the following forecasts are based on an assumed exchange rate of £0.70/€. The rise in revenue will be largely driven by electricity price increases, with which we pass through to the customer the rise in procurement costs. Furthermore, the fact that the Biblis nuclear power plant has come back online will have a positive impact on generation output. The reduction of our German grid fees by the German Federal Network Agency will have a counteracting effect.

1.11 Outlook for 2008

Outlook[1] € million	2007	2008 forecast vs. 2007
External revenue	42,507	Above previous year
EBITDA	7,902	At least matching previous year
Operating result	6,520	At least matching previous year
RWE Power	2,617	Up by more than 10%
RWE Dea	492	Up by more than 10%
RWE Supply & Trading	532	Below previous year
RWE Energy	2,355	Single-digit percent gain
RWE npower	724	Below previous year
Net income	2,659	Up by more than 10%
Recurrent net income	2,977	Up by more than 10%

1 Based on the new reporting structure; 2007 figures have been adjusted accordingly (see commentary on page 107).

Stable earnings trend despite higher CO_2 costs and grid regulation. The RWE Group's earnings are expected to maintain their high level. We anticipate being able to offset two key negative effects: stricter conditions underlying CO_2 emissions trading and further regulatory reductions of our German grid fees. In sum, these two factors will probably adversely affect earnings by roughly €1.5 billion compared with 2007. We expect to at least match 2007 levels in terms of both EBITDA and the operating result. Net income is anticipated to rise by more than 10%. Last year's figure was characterized by one-off effects. Recurrent net income, which is adjusted for one-off effects—the yardstick for determining the dividend—is also expected to rise by over 10%. As mentioned earlier, we will expand our €600 million efficiency-enhancement programme, which runs until 2010, over the course of the year. We expect these measures to contribute about €100 million to earnings in 2008. The point of focus is to improve the performance of our regulated German electricity and gas grid activities. In addition, we plan to improve the technical availability of our power plants.

Operating result by division:

RWE Power is expected to post another improvement in its operating result. We anticipate an increase of more than 10%. This will be driven by the higher electricity prices which we realized for our 2008 output over the past two years. RWE has already sold forward more than 90% of its German 2008 generation. In addition, we expect the two units of the Biblis nuclear power plant, which have gone back online, to have a positive effect on output. However, we will be faced with massive burdens stemming from CO_2 emissions costs. The German allocation plan for the period from 2008 to 2012 envisions a much reduced allocation of free emissions allowances. We expect that RWE Power will have to purchase an average of about 40% of the CO_2 certificates it needs on the market during this period, or obtain them via CDM/JI projects insofar as possible. The percentage shortage of emissions allowances in 2008 is expected to be clearly higher than the five-year average and to drop afterwards. We anticipate further adverse effects on earnings to come from higher hard coal and gas prices as well as increased staff and other costs in the current year.

From our present point of view, we expect RWE Dea to lift its operating result by more than 10%. This is based on the assumption that we will be able to realize higher gas and oil prices. However, production and operating costs are likely to rise.

The newly established RWE Supply & Trading is expected to close the year with an operating result that is lower than in 2007. This is because we do not anticipate that we will be able to match the unusually high trading result posted in 2007. We will probably grow the operating result of our gas midstream activities, following the startup losses incurred in the last year. But this business is not likely to break even yet.

Our forecast for RWE Energy envisions a single-digit percent increase in its operating result. This is based on the assumption that weather conditions will be normal and that our gas sales will thus be higher year on year. The most recent tariff cuts made by the German Federal Network Agency that apply to our German electricity and gas grids are a major burden. To limit the impact this will have on earnings, RWE Energy plans to implement further extensive cost reductions, focussing on Germany. In addition, we intend to improve earnings in our electricity and gas supply businesses. We will continue to pursue our value-oriented sales policy to this end. At the same time, we want to limit customer losses across market segments by developing innovative products. The range covers everything from fixed-price offers to private customers with terms of several years through portfolio management to auctions of power plant tranches to industrial enterprises and municipal utilities. Moreover, we will expand our web-based sales subsidiary eprimo.

From our present point of view, we do not expect RWE npower to match the operating result it recorded in 2007. We anticipate that the mounting cost of fuel—especially coal—will cause power generation margins to shrink. Furthermore, RWE npower will probably have to purchase approximately 25% of the CO_2 certificates it requires on the market. Staff costs are also expected to rise, especially because our capital expenditure on power plants will result in an increased need for manpower. The market environment of our electricity and gas sales businesses remains difficult, above all due to fierce competition and the recent rise in purchasing prices. We were the first energy company in the UK to raise household tariffs at the beginning of the year, increasing them by an average of 12.7% and 17.2% for electricity and gas, respectively. Gas transmission costs are expected to be much higher year on year, which would have a dampening effect on sales margins. In addition, we anticipate that a government programme that obliges UK utilities to support energy-saving measures taken by household customers will result in increasing burdens.

1.11 Outlook for 2008

Much higher dividend payment. Our dividend proposal for fiscal 2008 will probably be based on a payout ratio of between 70% and 80%. However, this will only happen if we successfully place the majority of the shares in American Water on the market over the course of the year. Otherwise, we will remain within the normal payout ratio of 50% to 60%. As before, the basis for calculating the payout ratio is recurrent net income, which is adjusted for one-off effects.

Capital expenditure on property, plant and equipment up year on year. We will clearly step up capital expenditure on property, plant and equipment in 2008. The greatest rise is planned for RWE Power. We want to start construction on the twin-unit hard coal power plants at Hamm, Germany, and Eemshaven, Netherlands, this year. Approval processes are underway for both these projects. Work on the gas-fired power station in Lingen, Germany, and on the dual-block lignite power plant in Neurath, Germany, has already progressed well. The commissioning of these two plants is scheduled for 2009 and 2010, respectively. Power station component costs have recently recorded a substantial rise. By securing components at an early stage, we were able to limit the rise in prices associated with our large-scale projects. Our upstream subsidiary, RWE Dea, will invest a lot more in gas production—above all in North Africa. RWE Energy has increased its capex budget substantially as well. We will spend some 80% of these funds on the grid business. Other funds have been earmarked for gas storage projects. RWE npower will also step up capital expenditure. Our main projects in the UK are the new gas-fired power stations in Staythorpe and Pembroke. Furthermore, we will build offshore wind farms off the coast of Wales. All in all, excluding American Water, the RWE Group's capital expenditure on property, plant and equipment will reach an order of magnitude of €6 billion in 2008. This would represent an increase of over 70% compared to 2007.

Net debt down year on year. Despite the dividend payment planned for April and the marked rise in capital spending, we will probably reduce net debt even further in the current financial year. The main drivers will be the expected high level of cash provided by operating activities and our assumption of being able to sell at least the majority of the shares in American Water by the end of 2008. Thanks to the good reputation we have as bond issuer, we always have access to short- and long-term financing sources. In 2008, €1.6 billion in bonds will mature.

Employee headcount: significant rise expected. This financial year, we anticipate that our workforce will expand by more than 1,500 employees. Substantial staff increases will be carried out by RWE Power and RWE npower.

Procurement: no major price risks expected for 2008. As mentioned earlier, we have already sold forward most of our 2008 electricity production. In principle, our approach involves purchasing the fuel required to generate contracted amounts when the supply agreements are signed, thus hedging fuel prices at the same time. This also applies to the purchase of CO_2 certificates. Therefore, costs incurred to purchase gas, hard coal and emissions allowances are largely determined by price developments on forward markets in the past, as is our electricity revenue. We have no fuel price risk exposure from lignite since we produce this fuel in our own opencast mines. Uranium required to run our nuclear power stations has been secured via long-term purchasing agreements. In the nuclear power generation sector, fuel procurement costs typically account for a small portion of total generation costs. However, it is only possible to make limited forecasts for our procurement costs since the actual usage of fuel by our power plants strongly depends on how we run them. This is in part determined by the development of spot prices on electricity and fuel markets, and power plant outages can also occur. We believe that savings can again be realized when purchasing materials and services in 2008. In addition, we expect to gain advantages from the combination of RWE Gas Midstream and RWE Trading resulting in the new RWE Supply & Trading.

Research and development: budget enlarged. We will spend far more than before on research and development (R&D). We plan to have R&D expenditure total in excess of €100 million in 2008 and trend upwards thereafter. As has been the case so far, we will focus on projects to improve efficiency and reduce emissions from electricity generation. More than two-thirds of our R&D budget have been earmarked for this. A milestone we will pass in 2008 is the commissioning of the first pilot lignite pre-drying plant in Niederaussem, Germany. We intend to extend the cooperative ventures with partners in the chemicals and plant engineering industries initiated last year, focussing on methods to separate carbon dioxide from flue gas. In addition, by launching RWE Innogy, we set the course towards intensifying R&D activities in the field of renewable energy. We are also working on our electricity grids. Steps we take in this area are directed to reducing voltage losses, intelligent grid usage and innovative energy measurement. Furthermore, we want to secure know-how in the field of nuclear energy and develop it over the long term. This will allow us to keep open the option of making use of this climate-friendly technology in a changing energy industry and social environment.

Forward-looking statements. This annual report contains forward-looking statements regarding the future development of the RWE Group and its companies as well as economic and political developments. These statements are assessments that we have made based on information available to us at the time this document was prepared. In the event that the underlying assumptions do not materialize or additional risks arise, actual performance can deviate from the performance expected at present. Therefore, we cannot assume responsibility for the accuracy of these statements.

Our Responsibility

2.0

2.1 Supervisory Board Report

Dear Shareholders,

In fiscal 2007, the Supervisory Board fulfilled all of the duties imposed on it by German law and the company's articles of association. It regularly advised the Executive Board on running the company and monitored business management measures. It was consulted on all decisions of fundamental importance to RWE. The Executive Board informed the Supervisory Board of all the material aspects of business developments, major events and transactions as well as of the current earnings situation, exposure to risk and risk management regularly, extensively and in a timely manner both in writing and verbally.

In the year under review, the Supervisory Board convened four meetings. All of the Supervisory Board members attended at least half the meetings. The average participation rate exceeded 95%. The Supervisory Board passed the resolutions required of it by law and the Articles of Association. The decisions were made on the basis of reports and draft resolutions submitted by the Executive Board. The Supervisory Board was informed of projects and transactions of special importance or urgency in a timely manner in-between meetings as well. When necessary, it was asked for approval by circular. The Chairman of the Supervisory Board was constantly in touch with the members of the Executive Board in order to immediately discuss events of material importance to the RWE Group's situation and development.

Debates in the plenum. One of the central topics of the Supervisory Board's debates was the planned IPO of American Water. We concerned ourselves with the status of the preparations for the placement of a majority of the shares in the US-based water utility, which had originally been planned for the end of 2007. The Supervisory Board was informed in detail of the postponement of the IPO, which was decided on November 14, 2007, with due regard to the rationale and the consequences for RWE.

Debates also centred on the extensive investment programme focussing on power plants, grid infrastructure, and the liquefied natural gas (LNG) business.

The sale of the investment in RAG AG was also the subject of several sessions. The Executive Board informed the Supervisory Board in detail of the agreement reached by the German federal government, the German states, and the trade union to discontinue the subsidization of the German hard coal mining sector in a socially acceptable manner. As a result of this agreement, the RAG Foundation had been established by RAG to cover the perpetual burden stemming from the mining sector and the non-coal activities were pooled in a company that is to be taken to the stock exchange. In this connection, RWE shed its 30.2% stake in RAG. In its meeting on September 20, 2007, the Supervisory Board approved the transfer of the investment to the RAG Foundation for a symbolic price of €1. In-depth debates on the advantages and disadvantages of this step were conducted by the Executive Board and the Supervisory Board in the run-up.

Dr. Thomas R. Fischer
Chairman of the Supervisory Board of RWE AG

Tighter energy policy setting. Another important subject of our debates was the development of framework conditions in the energy policy arena. Centre stage was taken by the shaping of the CO_2 emissions trading scheme in the second trading period (2008 to 2012). In addition, the Supervisory Board ensured that it was kept abreast of the progress made in the proceedings before the German Federal Cartel Office concerning the admissibility of factoring the price of CO_2 certificates into electricity tariffs and, above all, of the agreement reached with this authority on the discontinuation of the proceedings. The EU Commission's "Energy Package" was also debated extensively—above all as regards the desired unbundling of the ownership of the grid business from power utilities' other activities. Furthermore, the Supervisory Board discussed the reduction of German grid fees by the regulator and measures to limit earnings shortfalls. Special attention was also paid to the amendment to the German law against restraint of competition (GWB) and the consequences it may have for RWE. Moreover, the Executive Board held several consultations on the EU Commission's follow-up measures to the sector inquiry and to the Commission's investigation of potential antitrust violations on the European electricity and gas markets in 2006. In May and December of 2006, the Commission had conducted follow-up probes at RWE as part of this inquiry.

Other topics of deliberation. In its session on February 21, 2007, the Supervisory Board concerned itself with the succession planning for the Executive Board. Another issue debated at this meeting was the transfer of pension obligations via a Contractual Trust Arrangement with RWE Pensionstreuhand e. V. and the establishment of the RWE Pensionsfonds. In the meeting that took place on September 20, 2007, the Executive Board presented a report on the amendments to the Code adopted by the German Government Corporate Governance Code Commission. One of the new provisions stipulates that the Supervisory Board must form a nomination committee that is exclusively staffed with shareholder representatives responsible for presenting the Supervisory Board with the names of suitable candidates for election to the Supervisory Board. These individuals can be proposed to the Annual General Meeting as candidates for election to the Supervisory Board. We established such a nomination committee in our December 11, 2007, session.

Last financial year, the Supervisory Board also debated material capital expenditure and divestment projects and passed the necessary resolutions requiring approval. We had the Executive Board provide us with regular reports on the revenue and earnings situation, measures to reduce costs, and the development of energy prices. In our session on December 11, we concerned ourselves with the Executive Board's planning for 2008, the forecast for 2009 and 2010 and the long-term prognosis through 2017. We received detailed commentary in cases where there were deviations from plans and goals established previously.

Committees. The Supervisory Board has five committees. Their members are listed in the chapter on "Boards and Committees" on page 213. These committees are mainly charged with preparing issues and resolutions of the Supervisory Board meetings. In certain cases, they exert decision-making powers conferred on them by the Supervisory Board. At the Supervisory Board meetings, committee chairmen delivered in-depth reports on their respective work.

The ***Executive Committee*** convened twice in the 2007 financial year. Its activity primarily consisted of preparatory work for the Supervisory Board debates. The main subjects of the committee's preparations were the 2006 financial statements of the parent company and the Group, the dividend distribution policy, the company's strategic orientation, and the budget for 2008.

The ***Audit Committee*** convened four times in 2007. It discussed the interim results and financial statements at length and prepared the award of the audit contract to the independent auditor. A substantial amount of time was dedicated to discussing the findings of the audits conducted by Internal Auditing and the audit planning for 2007. Furthermore, the Committee debated the organization of compliance within the RWE Group, the effects of the transfer of assets to RWE Pensionstreuhand e.V. and RWE Pensionsfonds AG, the impact of the planned IPO of American Water on the balance sheet, the implementation of new accounting standards, the business models of individual divisions, and elements of the internal controlling system. The auditor of the financial statements took part in some of the debates.

The ***Human Resources Committee*** held three meetings. Debates primarily addressed the compensation system and the amount of remuneration paid to members of the Executive Board. Furthermore, the Committee prepared the Supervisory Board's personnel-related decisions.

As explained already, the Supervisory Board founded a new body, i.e. the ***Nomination Committee,*** in its meeting on December 11, 2007. This new committee will hold sessions whenever necessary. It was not necessary to convene it in the financial year under review.

In fiscal 2007, there was no reason to convene the ***Mediation Committee,*** which complies with Sec. 27, Para. 3 of the German Co-Determination Act, either.

Financial statements for fiscal 2007. The financial statements of the parent company, which were prepared by the Executive Board in compliance with the German Commercial Code; the financial statements of the Group, which were prepared in compliance with International Financial Reporting Standards (IFRSs); the combined review of operations for RWE Aktiengesellschaft and the Group; and the accounts were scrutinized by PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft and were issued an unqualified auditor's opinion. The auditors were elected by the AGM on April 18, 2007, and commissioned by the Supervisory Board to audit the financial statements of RWE AG and the Group. Documents supporting the annual financial statements, the annual report and the auditor's audit report were submitted to all the members of the Supervisory Board in good time. The Executive Board also commented orally on the documents in the Supervisory Board's balance sheet meeting of February 20, 2008. The appointed auditors attended the meeting, presented the material results of their audit, and were available to answer questions. The Audit Committee concerned itself in depth with the financial statements of RWE Aktiengesellschaft and the Group as well as audit reports during its meeting on February 19, 2008, with the auditor present; it recommended that the Supervisory Board approve the financial statements as well as the appropriation of profits proposed by the Executive Board.

The Supervisory Board thoroughly reviewed the financial statements of RWE Aktiengesellschaft and the Group, the combined review of operations for RWE Aktiengesellschaft and the Group, and the proposed appropriation of distributable profit. No objections were raised as a result of this review. As recommended by the Audit Committee, the Supervisory Board approved the auditor's results of the audit of both financial statements, and it adopted the financial statements of RWE Aktiengesellschaft and the Group for the period ended December 31, 2007. The 2007 annual financial statements are thus adopted. The Supervisory Board concurs with the appropriation of profits proposed by the Executive Board, which envisions a dividend payment of €3.15 per share.

Changes in personnel on the Supervisory and Executive Boards. Effective at the end of the day on August 15, 2007, the employee representative Sven Bergelin retired from the Supervisory Board. He was succeeded by Karl-Heinz Römer as of October 2, 2007. We thank Mr. Bergelin for his involved, constructive cooperation and for his commitment for the benefit of the company.

With effect from the end of the day on September 30, 2007, Harry Roels retired from his office of President and CEO of RWE Aktiengesellschaft. In its meeting on February 21, 2007, the Supervisory Board had resolved not to extend his appointment since he had reached the company's internal age limit. Thanks to his extensive international experience, Harry Roels' tenure was extraordinarily successful. The Supervisory Board has expressed its special thanks to Harry Roels for his entrepreneurial accomplishments. In its September 20, 2007 session, the Supervisory Board ended Harry Roels' tenure as member of the Executive Board early by mutual agreement with him and appointed Dr. Jürgen Großmann to the Executive Board of RWE Aktiengesellschaft and nominated him its Chairman as of October 1, 2007.

We thank the Executive Board and the RWE Group's entire staff for the work they did for the benefit of the company. With their commitment and expertise, they made a decisive contribution to ensuring that 2007 was another successful fiscal year for RWE.

Essen, February 20, 2008

The Supervisory Board

Dr. Thomas R. Fischer
– Chairman –

2.2 Corporate Governance

We accord high importance to good corporate governance. It fosters the trust of investors, customers and employees in our company management. The latest version of the German Corporate Governance Code, which was introduced in 2002, is our guiding principle. We have complied with the Code's recommendations unconditionally for five years.

Comprehensive implementation of the Code. The German Corporate Governance Code Government Commission adopted a number of amendments to the Code on June 14, 2007. Since then, it has recommended that provisions governing responsibilities within the Executive Board and majorities required to pass resolutions be included in the Rules of Procedure of the Executive Board. Another new recommendation proposes the establishment of a "nomination committee." It is to be staffed exclusively with shareholder representatives and suggest candidates to the Supervisory Board for candidate proposals made to the Annual General Meeting. Furthermore, the Code suggests that a cap be placed on severance payments made to exiting Executive Board members. Last, but not least, the Code addresses the issue of "compliance" and determines who within the company is responsible for compliance.

In its meeting on December 11, 2007, the Supervisory Board adopted the resolutions required to implement the Code's recommendations. The issue of compliance was assigned to the Audit Committee. This Committee has dealt with compliance in the past as well. Furthermore, the recommended nomination committee was formed. The Committee will monitor the national and international environments to identify available individuals and propose suitable successor candidates from this circle of people to the Supervisory Board. The Nomination Committee is composed of the Chairman of the Supervisory Board and the Human Resources Committee's shareholder representatives. No action was needed concerning the Code's recommendation to amend the Rules of Procedure of the Executive Board. RWE had already determined the responsibilities and the majorities required to pass resolutions.

We thus continue to put into practice all of the recommendations and—with just a few exceptions—the suggestions included in the current version of the Code. In February 2008, RWE issued an unqualified statement of compliance for the sixth straight time. Our listed Group company, Lechwerke AG, is putting the Code into practice, taking account of the specifics of its inclusion in the Group. Deviations have been disclosed in the statement of compliance.

The issue of compliance that is now addressed by the Code has long been a top priority at RWE. Besides the Code of Conduct, which was introduced in 2005, we also have an extensive set of rules. The Executive Board commissioned a renowned international law firm to review the RWE Group's compliance structures as part of a compliance audit that was conducted at the end of 2007. Based on the audit, the RWE Group's compliance structures meet high standards, which comply with applicable statutory regulations and generally accepted requirements in every respect. Recommendations were developed to improve compliance concerning certain details. We will analyze them and implement them in a suitable manner. In its meeting on February 19, 2008, the Supervisory Board's Audit Committee concerned itself with the results of the compliance audit and approvingly took notice of them.

Transparency is a core element of good corporate governance. It is necessary, inter alia, in cases where transactions concluded by the Executive Board may lead to conflicts of interest. The following issues are noteworthy as regards RWE:

- In fiscal 2007, no material transactions were concluded between RWE or a Group company and an Executive Board member or related party. Furthermore, no contracts were concluded between RWE AG and members of the Supervisory Board. Executive Board and Supervisory Board members had no conflicts of interest.

- Executive Board members again purchased RWE common shares (ISIN DE 007037129). No sales occurred in the year under review. We reported the securities dealings in accordance with Sec. 15a of the German Stock Corporation Act (WpHG) and distributed this information throughout Europe in compliance with statutory regulations. The following is a breakdown of the transactions:

Transaction date	Name	Reason for mandatory disclosure/function	Type of financial instrument	Transaction (purchase/sale)	Price per share/€	Number of shares	Total volume €
03/30/2007	Harry Roels	Member of the Executive Board	RWE common share	Purchase	77.1079	1,919	147,970.06
03/30/2007	Berthold Bonekamp	Member of the Executive Board	RWE common share	Purchase	77.1079	1,440	111,035.38
03/30/2007	Alwin Fitting	Member of the Executive Board	RWE common share	Purchase	77.1079	1,440	111,035.38
03/30/2007	Dr. Ulrich Jobs	Member of the Executive Board	RWE common share	Purchase	77.1079	1,440	111,035.38
03/30/2007	Dr. Rolf Pohlig	Member of the Executive Board	RWE common share	Purchase	77.1079	240	18,505.90
03/30/2007	Dr. Klaus Sturany	Member of the Executive Board	RWE common share	Purchase	77.1079	540	41,638.27
03/30/2007	Jan Zilius	Member of the Executive Board	RWE common share	Purchase	77.1079	600	46,264.74
11/16/2007	Dr. Jürgen Großmann	Member of the Executive Board	RWE common share	Purchase	87.0900	20,000	1,741,800.00

- The number of shares in the company and related financial instruments directly or indirectly held by members of the Executive and Supervisory Boards is below 1% of the shares issued by RWE (Item 6.6 of the Code).

Compensation report (part of the Review of Operations). RWE has been publishing the compensation of its Executive and Supervisory Boards by individual since 2003. In fiscal 2006, this was done in a separate compensation report as part of the corporate governance report for the first time. The 2007 Compensation Report takes into account the provisions of the version of the

German Commercial Code that was amended as a result of the German Board of Management Compensation Disclosure Act (VorstOG) and the German Adoption Directive Implementation Act and fully complies with the recommendations of the German Corporate Governance Code. The Compensation Report is part of the Combined Review of Operations.

Executive Board Compensation:

Compensation structure. The compensation of the Executive Board members and the structure of such are established by the Human Resources Committee of the Supervisory Board and reviewed on a regular basis. The existing compensation system ensures that the Executive Board members are compensated in a manner commensurate with their activities and responsibilities. Besides their personal performance, this takes into account the company's business situation as well as its performance and prospects for the future.

Short-term compensation components. The total cash compensation consists of a non-performance-based, fixed component and a variable, performance-related component. The total cash compensation breaks down into roughly 40% for the fixed component and 60% for the variable component. The variable component consists of a company bonus, accounting for 70%, and an individual bonus, accounting for 30%. Through the 2006 fiscal year, the company bonus was based equally on the Group's budgeted figures for value added and free cash flow. Since 2007, we have exclusively used the Group's budgeted value added as a basis for determining the company bonus. If the figures budgeted for the fiscal year in question are achieved, the degree to which the target has been achieved is 100%. The degree to which the target has been achieved as regards the company bonus can amount to between 50% and a maximum of 150%. The personal bonus depends on the achievement of the goals agreed between the Chairman of the Supervisory Board and each Executive Board member at the beginning of the financial year. The maximum degree to which this target can be achieved is 120%.

Above and beyond this, Executive Board members receive non-cash compensation and other compensation, consisting primarily of sums reflecting the use of company cars according to German fiscal guidelines and accident insurance premiums.

Compensation also includes payment for exercising Supervisory Board mandates held by Executive Board members at affiliates. Compensation for mandates is credited to the variable compensation.

Furthermore, on taking office, Dr. Rolf Pohlig received a lump sum payment of €480,000 as compensation for benefits from his former employer, to which he is no longer entitled since he joined RWE.

The short-term compensation components paid to members of the Executive Board for fiscal 2007 is as follows:

Short term Executive Board compensation in 2007	Non-performance-based compensation		Performance-based compensation		Non-cash and other remuneration		Payment for exercise of mandates[1]		One-time bonuses		Total	
€ '000	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006	2007	2006
Dr. Jürgen Großmann (as of October 1, 2007)	675	-	959	-	11	-	23	-	0	-	1,668	-
Harry Roels (until September 30, 2007)	1,050	1,400	1,739	2,354	24	24	124	120	0	0	2,937	3,898
Berthold Bonekamp	680	680	1,058	1,087	68	52	85	93	0	0	1,891	1,912
Alwin Fitting	587	450	925	728	17	15	61	32	0	0	1,590	1,225
Dr. Ulrich Jobs (as of April 1, 2007)	300	-	487	-	14	-	17	-	0	-	818	-
Dr. Rolf Pohlig	700	-	1,155	-	29	-	35	-	480	-	2,399	-
Dr. Klaus Sturany (until April 30, 2007)	333	1,000	462	1,305	24	37	11	80	0	0	830	2,422
Jan Zilius (until April 30, 2007)	227	680	374	1,111	27	54	21	69	0	0	649	1,914
Total	**4,552**	**4,210**	**7,159**	**6,585**	**214**	**182**	**377**	**394**	**480**	**0**	**12,782**	**11,371**

1 Income from the exercise of mandates is added to variable compensation.

The short-term compensation components include a total of €1,900,000, which was paid for the exercise of management board mandates at subsidiaries. These sums were paid through the respective subsidiaries.

Long-term incentive compensation. In addition—with the exception of the Chairman of the Executive Board, Dr. Jürgen Großmann—performance shares were awarded to members of the Executive Board as part of the Beat 2005 long-term incentive plan ("Beat" for short). A condition for the granting of performance shares to the Executive Board members is an investment by the Board members in RWE shares. This investment is equal to one-third of the value of the performance shares granted after taxes. The shares must be held for the respective Beat tranche's entire three-year waiting period. Any necessary notifications of directors' dealings in relation to this were submitted and published.

The "Beat" programme supplements the compensation system with a long-term incentive component by rewarding the sustainable contribution made by executives to the company's success. The company's performance is measured using Total Shareholder Return (TSR) of RWE shares, which covers both the development of the share price and reinvested dividends. The payout factor is determined by comparing RWE's TSR with the TSR of other companies in the Dow Jones STOXX Utilities Index.

Executives entitled to participate in Beat receive a conditional allocation of performance shares every year. A performance share consists of the conditional right to receive a pay-out in cash following a waiting period of three years. However, a payout only takes place if, on conclusion of the waiting period, the RWE share's performance exceeds the performance of 25% of the companies in the peer group, measured in terms of their index weighting as of the inception of the programme. In consequence, the decisive factor is not only RWE's position among the companies in the peer group, but also which of the companies RWE outperforms.

Payment corresponds to the average RWE share price during the last 20 trading days prior to expiration of the programme, the number of conditionally allocated performance shares, and the pay-out factor. Payment under the 2005 tranche is limited to three times the value of the performance shares as of the grant date and, under the 2006 and 2007 tranches, to double (for Executive Board members one-and-a-half times) the value of the performance shares as of the grant date.

Performance shares granted under Beat in the year under review break down as follows:

Long term incentive share-based payment	Beat: 2007 tranche	
	No.	Fair value upon grant € '000
Dr. Jürgen Großmann (as of October 1, 2007)	0	0
Harry Roels (until September 30, 2007)	40,016	1,000
Berthold Bonekamp	30,012	750
Alwin Fitting	30,012	750
Dr. Ulrich Jobs (as of April 1, 2007)	30,012	750
Dr. Rolf Pohlig	30,012	750
Dr. Klaus Sturany (until April 30, 2007)	11,255	281
Jan Zilius (until April 30, 2007)	12,505	313
Total	**183,824**	**4,594**

Prior-year allocations. In the year under review, the Executive Board members held performance shares from the Beat programme's 2005 and 2006 tranches. These allocations are not part of total compensation for the 2007 financial year. Instead, they are part of total compensation for fiscal 2005 and 2006 and as such are presented in the compensations reports for these two prior years. The following overview of these allocations is voluntary and aims to convey a complete picture of the compensation history.

Long term incentive share-based payment	Beat: 2005 tranche	
	No.	Fair value upon grant € '000
Harry Roels	161,100	3,000
Berthold Bonekamp	53,700	1,000
Alwin Fitting	10,000	186
Dr. Klaus Sturany	80,600	1,501
Jan Zilius	53,700	1,000
Total	**359,100**	**6,687**

Long term incentive share-based payment	Beat: 2006 tranche	
	No.	Fair value upon grant € '000
Harry Roels[1]	114,416	2,000
Berthold Bonekamp	57,208	1,000
Alwin Fitting	57,208	1,000
Dr. Klaus Sturany	57,208	1,000
Jan Zilius	38,158	667
Total	**324,198**	**5,667**

1 €1,000,000 of the €3,000,000 originally granted expired in fiscal 2007 since the grant prerequisites were not met.

Total compensation. In total, the Executive Board received €12,782,000 in short-term compensation components in fiscal 2007. In addition to this, long-term compensation components from the 2007 tranche of the Beat programme amounting to €4,594,000 were allocated. Total compensation of the Executive Board for fiscal 2007 thus amounts to €17,376,000. As planned, in fiscal 2007, no payments were made based on performance shares allocated in the preceding year.

Employment termination benefits:

Pension commitments. The members of the Executive Board—with the exception of its Chairman, Dr. Jürgen Großmann—received pension commitments (direct commitments), which grant them entitlement to a life-long pension and surviving dependants' benefits. These benefits are due in the event of retirement upon reaching the age limit, permanent disability, death and early termination or non-extension of the employment contract occasioned by the company. The amount of qualifying income and the level of benefits determined based on the duration of service is taken as a basis for each member's individual pension and surviving dependants' benefits. Profit participation and other fringe benefits are not factored into the pension. The ceiling for pension benefits for members of the Executive Board is 60% of the last qualifying income on the day before they reach the age limit. The widow's pension amounts to 60% of her husband's pension, the orphan's pension amounts to 20% of the widow's pension. Vested old-age pension benefits do not expire. The amount of the old-age pension and the surviving dependants' benefits are reviewed every three years, taking account of all major circumstances, with due regard to the development of the cost of living. Due to earlier provisions, there are some differences in the pension commitments in terms of the calculation of the level of benefits, the crediting of other pensions and benefits, and the adjustment mode selected for pensions and surviving dependants' benefits.

In the event of an early termination or non-extension of an employment contract, Executive Board members shall only receive payment if the termination or non-extension was occasioned by the company and effected without due cause. In such cases, Executive Board members start receiving pension payments when they leave the company, but no earlier than on completion of their 57th year of age.

The service cost and past service cost of pension commitments in fiscal 2007 totalled €1,913,000. As of the end of the year under review, the present value of the defined benefit obligation was €9,104,000. The following is a breakdown of service costs and the present value of pension benefits, taking into account both age and service life.

Pensions		Predicted annual pension on reaching the company age limit (60 years) [1] € '000		Current service cost € '000		Past service cost [2] € '000		Defined benefit obligation € '000	
	Age	2007	2006	2007	2006	2007	2006	2007	2006
Berthold Bonekamp	57	324	324	152	161	0	0	3,218	3,646
Alwin Fitting	54	283	220	134	220	0	0	2,658	2,443
Dr. Ulrich Jobs (as of April 1, 2007)	54	156	-	116	-	0	-	1,717	-
Dr. Rolf Pohlig	55	252	-	73	-	1,438	-	1,511	-
				475	**381**	**1,438**	**0**	**9,104**	**6,089**

1 Based on compensation qualifying for pensions as of December 31, 2007.
2 Figures shown as past service costs reflect years of service for prior employers.

As regards Executive Board members, vested pension benefits from earlier employment relationships and years of service for previous employers which have been recognized are credited to the company's pension payments by contractual arrangement.

Instead of a pension commitment, Dr. Jürgen Großmann will receive an annual €2,000,000 in pension capital for use at his discretion. It will be paid for the first time one year after his taking office.

Change of Control. Before the last amendment to the German Corporate Governance Code, the Chairman of the Executive Board, Dr. Jürgen Großmann, was granted a special right of termination in the event of a change of control. A change of control occurs when more than 30% of the voting rights in a company are controlled by a shareholder or a group of shareholders acting jointly, who do not represent the majority ownership of an entity under public law. On exercise of the special right of termination, Dr. Jürgen Großmann shall receive a one-time payment that covers all of the remuneration due until the agreed expiry of his employment contract, including the contractually agreed pension capital.

In the event of a change of control, all the performance shares granted to the Executive Board and entitled executives shall expire. Instead, a compensatory payment shall be made, which shall be determined when the takeover offer is made. The amount shall be in line with the price paid for RWE shares at the time of the takeover. This shall then by multiplied by the final number of performance shares. Performance shares shall also expire in the event of a merger with another company. In this case, the compensatory payment shall be calculated based on the expected value of the performance shares at the time of the merger. This expected value shall be multiplied by the number of granted performance shares that corresponds to the ratio of time during the waiting period until the merger to the waiting period for the performance shares.

Other commitments. By mutual agreement, Harry Roels ended his mandate as Chairman of the Executive Board early as of September 30, 2007. As contractually agreed, Harry Roels will receive all the payments and benefits due to him from his employment contract, which ended on January 31, 2008, consisting of the fixed compensation as well as the bonus and company car benefits. The payment required on this basis of calculation in order to fulfil the employment contract, which was originally concluded with a date of expiry of January 31, 2008, amounts to €467,000. The bonus for the period from January 1 to January 31, 2008, which has already been established, amounts to €828,000. With effect from February 1, 2008, Harry Roels is entitled to a company pension in accordance with the contractual arrangement. The performance shares granted until the agreed exit date shall remain valid, in line with the plan conditions.

Supervisory Board compensation. The compensation of the Supervisory Board is set forth in the bylaws and is determined by the Annual General Meeting. Supervisory Board members receive a fixed compensation of €40,000 per fiscal year for their services at the end of each fiscal year. The compensation increases by €225 for every €0.01 by which the dividend exceeds €0.10 per common share.

The Chairperson of the Supervisory Board receives three times and the Deputy Chairperson receives twice the aforementioned amount. If a committee has been active at least once in a fiscal year, committee members receive one-and-a-half times the total compensation and the committee chairperson receives twice the total compensation. If a member of the Supervisory Board holds several offices on the Supervisory Board of RWE AG concurrently, he or she receives compensation only for the highest-paid position. Out-of-pocket expenses are refunded.

Supervisory Board compensation	2007 base compensation		2007 committee compensation		Total	
€ '000	Fixed	Variable	Fixed	Variable	2007	2006
Dr. Thomas R. Fischer, Chairman	120	206	0	0	326	350
Frank Bsirske, Deputy Chairman	80	137	0	0	217	233
Dr. Paul Achleitner	40	69	20	34	163	175
Sven Bergelin (until August 15, 2007)	25	43	0	0	68	84
Werner Bischoff	40	69	20	34	163	126
Carl-Ludwig von Boehm-Bezing	40	69	40	69	218	233
Heinz Büchel	40	69	20	34	163	126
Dieter Faust	40	69	20	34	163	175
Simone Haupt	40	69	20	34	163	159
Heinz-Eberhard Holl	40	69	20	34	163	175
Dr. Gerhard Langemeyer	40	69	20	34	163	175
Dagmar Mühlenfeld	40	69	6	10	125	116
Erich Reichertz	40	69	0	0	109	84
Dr. Wolfgang Reiniger	40	69	10	17	136	175
Günter Reppien	40	69	20	34	163	175
Karl-Heinz Römer (since October 2, 2007)	10	17	0	0	27	0
Dagmar Schmeer	40	69	0	0	109	46
Dr. Manfred Schneider	40	69	20	34	163	175
Dr.-Ing. Ekkehard D. Schulz	40	69	20	34	163	126
Uwe Tigges	40	69	20	34	163	175
Prof. Karel Van Miert	40	69	0	0	109	116
Total	**915**	**1,576**	**276**	**470**	**3,237**	**3,199**[1]

1 Figure adjusted; Supervisory Board members who retired from office as of January 1, 2007, are not included.

In total, the emoluments of the Supervisory Board amounted to €3,237,000. in fiscal 2007. Additionally, certain Supervisory Board members were paid compensation totalling €268,000 for exercising mandates at subsidiaries.

Statement of compliance in accordance with Sec. 161 of the German Stock Corporation Act.
Following an orderly audit, the Executive and Supervisory Boards of RWE AG issued the following declaration of compliance:

RWE Aktiengesellschaft complies with all of the recommendations of the German Government Corporate Governance Code Commission issued in the July 20, 2007, version of the Code. Likewise, from the last statement of compliance on February 21, 2007, to July 20, 2007, RWE Aktiengesellschaft has complied with all of the recommendations of the version of the Code issued on July 24, 2006, and since July 21, 2007, has complied with all of the recommendations of the July 20, 2007, version of the Code.

Essen, February 20, 2008
RWE Aktiengesellschaft

On behalf of the Supervisory Board	On behalf of the Executive Board	
Dr. Thomas R. Fischer	Dr. Jürgen Großmann	Dr. Rolf Pohlig

2.3 Workforce

Long-term personnel planning and executive resource development

Excessive ageing, a declining population and the lack of budding professionals: These are the buzzwords that describe our society's demographic change. The upshot are substantial risks for the German economy—not only in the distant future, but today as well. RWE is rising to these challenges. In 2007, our HR activities centred on refining long-term personnel planning and retention programmes, training young adults, and the systematic promotion of our employees.

We are developing strategies to cope with demographic change. Germany's population is ageing and shrinking. When compared on a European level, our largest market suffers from the ramifications of demographic change. RWE is affected by the changes caused by current developments in more ways than one. Based on the RWE Group's present age structure, the number of employees that leave the company due to retirement can be expected to rise significantly in the next seven to ten years. This will result in a loss of expertise and experience. In addition, there will be a reduction in the number of suitable job applicants. The employment market is already much more fiercely contested than just a few years ago. Therefore, we are developing programmes with which we can systematically assess our future personnel needs. The results serve as a basis on which to plan staff deployment to suit our needs and to guarantee the permanent availability of qualified job candidates.

In the medium term, the rise in the retirement age will result in longer working lives. This will place new demands on company health management: Prevention and health maintenance will become increasingly important in our society. This is why RWE has developed a comprehensive offering aiming to improve employee fitness and prevent illness, which is being expanded continuously.

Another consequence of demographic change is that the work life balance becomes more important and that the definition of the role women play in the workforce is being redefined. Against this backdrop, RWE initiated several measures, including the expansion of the "lifeandfamily" audit to include additional areas within the company. In so doing, we would like to help our employees reconcile their working and family lives better.

We train more young adults than we need. Training and integrating the young generation in the working world is another important step toward coping with demographic change. RWE has been strongly involved in vocational training for numerous years, thus securing a pool of qualified budding professionals. In addition to the traditional curriculum, our training programmes offer a host of ways to gain further qualifications. Our apprentices can participate in demanding project work or complete part of their apprenticeships in one of our companies outside Germany. We also enable and promote the combination of a training programme with a course of study in a variety of fields. RWE employs a total of more than 2,900 apprentices. Every year, roughly 900 teenagers embark on a training programme with us—in any one of about 65 training sites where they can choose among more than 50 professions. We are thus offering ten times as many apprenticeships as required to cover our own needs.

We promote our employees purposefully. In our quest to support the development of outstanding talent among non-executive staff throughout the Group and to plan long-term development options more accurately, we expanded the assessment of their potential. We believe that employees who have been classified as having "multi-level potential" can make more than just one vertical career move within a manageable timeframe. Our comprehensive potential analysis is the tool used throughout the Group to validate multi-level status. This process involves outside consultants, executives and human resources specialists from several RWE Group companies, who work as observers and appraisers. The objective is to promote talent by identifying individual strengths and weaknesses and providing feedback on our findings. This analysis of potential is then used as a basis from which development measures are derived. Participants with confirmed multi-level status are accepted into the "RWE Corporate Talent Programme" where they are promoted further.

Furthermore, we want to have an extensive overview of our staff's qualifications. Our qualification management system is a tool that enables us to record and control this data, which is important when it comes to ensuring our company's success. Our staff can enter their qualifications into the system themselves, based on a groupwide, uniform catalogue that includes all of the qualifications that are of relevance to the Group. In the future, a list of requirements will be drawn up for every position. By comparing employee skills with the job requirements, we can identify necessary action and initiate special personnel development measures early on. At the same time, this tool puts us in a position to identify personnel-related risks and take countermeasures as soon as possible.

Employee shares—sharing success. Our staff should be given the opportunity to partake of their company's success. Part of their compensation is already linked to the RWE Group's economic development. White collar workers also benefit from individual, performance-based compensation. Furthermore, our workforce can subscribe employee shares under favourable conditions. In 2007, a total of 22,062 staff members purchased about 457,000 shares, which corresponds to nearly 21 shares per participant. Costs related to the issuance of employee shares amounted to €13.3 million in the year under review. Our labour force currently owns some 2% of RWE's subscribed capital.

2.3 Workforce

We detect and avoid risks at work. Last year, we made inroads into the continuous process of improving occupational safety. This was triggered by the RWE Group's occupational safety and health protection policy, which was adopted in 2006. Our objective is to ensure that all our employees return home in the same physical condition as when they leave for work. The decline in the number of accidents witnessed for years proves that our efforts have paid off. We are pleased about this positive trend: The number of work-related incidents dropped for the sixth straight year. Compared with 2006, the number of work-related accidents causing more than a day of absence in 2007 declined from 7.7 to 6.1 per million work hours.

Unfortunately, however, in the year under review, nine people died as a result of work-related accidents, eight of whom worked for outside companies. An especially severe work-related incident occurred on the construction site of the lignite-fired power plant in Neurath, Germany, in October 2007. The accident claimed the lives of three people and hurt six others, some of whom were severely injured. For reasons as yet unknown, several tons of support structures attached to the large boiler scaffolding loosened and plummeted from a great height. The cause of the accident is being analyzed. In the future, we will provide the external contractors we hire with even stronger support in matters concerning safety at work.

Development of work and business travel accidents[1]	2007	2006	2005
RWE Power	8.8	9.3	10.9
RWE Trading	0.0	0.0	0.0
RWE Dea	1.1	2.5	4.3
RWE Energy	6.8	9.3	13.3
RWE Gas Midstream	0.0	–	–
RWE npower	2.1	1.6	2.4
RWE Systems	4.0	6.6	5.9
RWE AG	3.2	0.0	0.0
RWE Group	**6.1**	**7.7**	**10.3**

1 Number of work accidents per million work hours resulting in an absence of more than one day.

2.4 Sustainability

Setting the stage for success the day after tomorrow

What can we do to combat climate change without jeopardizing electricity supplies? Will RWE have access to enough skilled labour 20 years from now? How can our employees reconcile work and life better? Sustainable action requires one to ask these very questions. Our answers are designed to raise the acceptance of RWE among our customers, staff and investors, while setting the stage for economic success the day after tomorrow.

Our sustainability strategy. RWE has been rising to the challenges of sustainable management for years. We already have a successful track record: For example, we have a system for recording, assessing and controlling the demands that society places on us. The organizational structures of sustainability management have become firmly cemented in our company, and maintaining dialogue with stakeholder groups is part of our daily business.

Environmental protection and societal issues are integral components of our target-setting system. This gives rise to a host of fields of activity, some of which have recently gained significant importance. Climate change, the rise in energy prices and the finite nature of resources are perceived as ever-larger challenges for utilities. In addition, topics concerning the industry as a whole such as demographic change are increasingly coming to the forefront. In the financial year that just came to a close, we took this as an opportunity to refine our sustainability strategy. The outcome was the definition of ten fields of activity on which we intend to concentrate our work in the years ahead. This chapter will give you a brief introduction to each of these fields of action. Detailed information will be included in RWE's sustainability report entitled “Our Responsibility,” which will appear in April 2008.

(1) Climate protection. We have already provided a detailed report on the special significance climate protection has for RWE and on our initiatives to reduce carbon dioxide emissions on pages 2 et seqq. and 38 et seqq. The main points of our CO_2 avoidance strategy are the modernization of our power plant portfolio, the expansion of installed renewable energy capacity, climate protection projects in developing and newly industrializing countries, and the engineering of a climate-friendly coal-fired power plant with CO_2 storage. Furthermore, we are proponents of the extension of nuclear power plant lifetimes. The degree to which these efforts are successful will influence whether the ambitious climate protection goals set by policymakers on our core markets—Germany and the UK—can be achieved.

(2) Energy efficiency. The climate can only be protected effectively if the required change in mindset permeates to people's living rooms and offices. Consumers must also play their part by making careful use of energy. Our nationwide media campaign entitled "An Idea from RWE" provides an important stimulus for this. The products and services advertised by the campaign are designed to make it easier for our customers to reduce power usage considerably, thereby providing the environment with some relief. The campaign is part of the €150 million energy efficiency programme we launched in the spring of 2007. The programme runs the gamut from information activities conducted at schools to campaigns promoting more widespread use of heat pump technology and a well funded award recognizing the most energy-efficient commercial property. Since the beginning of 2008, city halls in communities located in RWE's German sales regions have been able to take advantage of our free energy check-ups. We thus trigger the refurbishment of municipal buildings. A similar offer from RWE is available to hospitals and other welfare institutions. Moreover, RWE intends to realize savings in street light operation by accelerating the retrofitting of street lights with energy-efficient lamps.

(3) Security of supply. As a major power utility, we are obliged to provide electricity and gas affordably and reliably from a long-term perspective. To this end, RWE draws on a wide-ranging generation portfolio, comprising nuclear, coal, gas and renewable energy. The availability of coal and nuclear power has been secured over the long term. We can cover demand for several decades with our German lignite production alone. We aim to secure a more diversified and flexible portfolio of natural gas. Our projects dealing with the liquefaction, shipping and regasification of gas are designed to make a contribution to this cause. Our investment in the Nabucco consortium has the same thrust. It involves the construction of a pipeline that is to connect Central Europe with Caspian and Iranian gas reserves, which would reduce our dependency on gas imports from Russia.

(4) Research and development. The more modern power plants we have, the more economically we can make use of scarce resources and the kinder our electricity generation is to the environment. Research and development (R&D) is thus a cornerstone of our sustainability strategy. In the years ahead, RWE will significantly increase R&D expenditure, which amounted to €47 million in 2007. In so doing, we will focus on ways to improve efficiency and reduce emissions in our coal-based electricity generation. In addition, we want to make a contribution to using renewable energy more effectively. Our attention is not directed to the continued development of existing methods alone. We also monitor emerging technologies and examine them to determine the potential they may have for us. Detailed information on the RWE Group's research and development work is provided on page 92 et seq. and on the internet at www.rwe.com/RandD.

(5) Pricing. Our customers expect fair prices, followed by good service and useful products. People often fail to understand why electricity tariffs are raised, even if the increases are based on the fact that the utilities bear higher costs, which they cannot influence. Some claim that tariff increases are arbitrary. We know that it is impossible to regain customer trust with objective arguments alone. What one really needs to do is to come up with an entire set of measures. The energy pact for Germany proposed by RWE's CEO at the end of 2007, aiming to improve dialogue among policymakers, society and power utilities, was a forward-looking step. The new loyalty power offering including a flat rate for three years targets private customers in Germany looking for long-term price stability. We also sell electricity at favourable terms via the internet. In concert with our industrial customers, we have developed customized model contracts that limit economic risks associated with rising energy prices. This is also the intention behind our offering industrial enterprises and municipalities stakes in new power plants in order to secure shares of capacity.

Furthermore, our electricity pricing ensures enhanced transparency: This is why we launched a new online information offering in January 2008. RWE publishes real-time data on current power production on the internet—for every power plant location as well as combined by primary energy source and fuel. Up-to-date data on electricity fed into the grid from power plants are of significant importance to all market participants such as power producers and suppliers, grid operators and energy traders. But our private customers should also be able to obtain a clear picture of the items that make up their electricity bills. We set up a website at "www.rwetransparent.com" for them. It contains a host of information in clear and understandable language. Electricity price components are explained under a dedicated menu item.

(6) Social responsibility. Commercial success is not the only yardstick of performance. Proven social responsibility is another good measure. We do whatever we can to act as a reliable partner in the regions in which RWE is active. This holds true especially regarding new power plants: We have awarded some €1 billion in contracts to companies located in North Rhine-Westphalia just for the construction of the new twin-unit lignite-fired power station in Neurath, which is close to Cologne, Germany. Our day-to-day business is another way besides large-scale projects in which we contribute to creating value in regions in which we operate, e.g., by contracting services, procuring commodities and consumables, and employing people in our operating units. We take our responsibility for young people very seriously. For instance, in the financial year under review, we trained ten times as many young adults as required to meet our own needs.

Furthermore, we promote our employees' social commitment. "People Make It Possible" is the motto of RWE Companius, an umbrella organization for our social volunteers in Germany, which was established in September 2007. It pools the regional activities with which we have been supporting the outstanding charity work done by RWE employees for years. Staff members can qualify for €500 and—in special cases—even up to €5,000 to fund their projects, under the condition that they help children and young adults and have to do with schooling, social welfare, culture, or sports. This year, we will expand RWE Companius' offering to include all of our companies on the European Continent. In the UK, RWE npower has a long-standing tradition of promoting its employees' charity work. More than 10% of the workforce did some form of social volunteering in 2007. RWE npower's social citizenship encompasses major fund raisers, e.g., for the Macmillan Cancer Foundation as well as programmes for the underprivileged, which help them improve home heating. In addition, RWE npower works closely together with schools and universities, seeking to re-kindle the interest of pupils and students in technology and natural sciences and thus contribute to securing future generations of technological experts.

(7) Supply chain. Safeguarding human rights, humane working conditions and the war against corruption may be a matter of course for us, but does the same hold true for our suppliers? The public expects us not to limit our sense of responsibility to the confines of our plant premises. By implementing a systematic supplier management system, we want to ensure that our business relationships with external partners are in line with our groupwide code of conduct. According to the code, we are forbidden from maintaining business relationships with suppliers who are publicly known to infringe the fundamental ethical principles set forth by the UN "Global Compact" initiative. The focal point of our supplier management is the purchase of fuel—above all hard coal—by RWE Trading. We have been subjecting our suppliers to intensive scrutiny since 2007. Risks are much lower when procuring plants and complex components. This is because suppliers of these products almost exclusively come from OECD member states. This means that fundamental ecological and social standards are generally complied with.

(8) Demographic development. In most of the European markets in which RWE is active, low birth rates are causing the population's average age to rise. This poses manifold challenges for companies such as RWE. Most importantly, it is becoming more difficult for us to cover our need for young, up-and-coming professionals over the long term. Issues such as the work life balance and improving career opportunities for women are also gaining significance as a result of the change in demographics. Our "Workforce" chapter explains on page 128 et seq. how we tailor or human resources management work to tackle these challenges.

(9) Occupational and health safety. Occupational safety has on a long-standing tradition at RWE. Since its implementation is strongly dependent on operational activity, it is first and foremost our operating management companies which are called upon in this regard. In order to make standards and results comparable across divisions, RWE's Executive Board adopted a groupwide occupational health and safety policy in August 2006. Among the objectives is to coordinate goals and measures. As explained on page 130, we have reduced the accident rate significantly in the past. We include employees of external companies doing contract work for us in our occupational safety management system. Nevertheless, nine people died as a result of work-related accidents in the year under review, eight of whom worked for outside companies. We took this as an occasion to increase our efforts to ensure that our employees display safety-aware behaviour. All divisions committed themselves to take further steps to improve occupational safety. For example, accident number reductions are to be included in the target agreements struck with executives. RWE has also launched the first series of initiatives in the field of health management, including a comprehensive prevention campaign.

Environmental expenditure	Expenses		Capital expenditure		Total	
€ million	2007	2006	2007	2006	2007	2006
Clean air	239	212	90	138	329	350
Nature and landscape protection	76	73	3	3	79	76
Water protection	184	182	13	14	197	196
Waste disposal	196	196	4	5	200	201
Noise abatement	10	12	2	1	12	13
Brownfield sites, soil contamination	6	15	1	1	7	16
Climate protection	130	-[1]	817	-[1]	947	-[1]
Total	**841**	**690**	**930**	**162**	**1,771**	**852**

1 We recorded climate-protection expenditure after 2006 due to changes in the German environmental statistics law.

(10) Environmental protection. We have already written about the efforts we undertake to reduce the effects our production operations have on the climate. Environmental protection has a number of additional facets that are factored into our decision-making and work processes: Thanks to the use of modern filtering units in our power stations and extensive noise-abatement and dust-protection measures taken in our opencast lignite mines, we have been complying with the strictest of environmental requirements for many years. It is with the same degree of care that we dedicate ourselves to the conservation of nature and landscapes. This is reflected, e.g., by our ecologically balanced line maintenance and the recultivation of former mining land. In fiscal 2007, we spent €1,771 million on environmental protection. For the first time, these figures include climate-protection measures. They accounted for more than half of the expenditure. Climate-protection measures had not yet been factored into the comparable figure for 2006 (€852 million). Numerous investment projects aimed at improving environmental protection besides our capital expenditure. One highlight is the retrofitting of the hard coal-fired power plant in Aberthaw, UK, with a flue gas desulphurization unit.

RWE—a sustainable investment. Financial markets expect companies to adhere to ever-higher transparency standards. This also applies to activities in the field of sustainable management. We gladly fulfil their wishes by publishing a comprehensive sustainability report every two years that has been reviewed by our auditors. Supplementary and late-breaking information is available on the web at "www.rwe.com/responsibility." At presentations and in one-on-ones, we regularly conduct dialogue with investors who put together their portfolios using sustainability as a criterion. These investors are especially interested in learning how we manage risks arising in connection with our carbon dioxide emissions. We report on this issue within the scope of the Carbon Disclosure Project, which is supported by the world's leading banks and investment institutions.

The efforts we undertake to ensure sustainable management are rewarded. Proof of this can be found in the fact that RWE was listed in the renowned Dow Jones Sustainability group of indices (DJSI) for yet another year in September 2007. Selections are made based on economic, ecological and social criteria. RWE is in the DJSI World and European DJSI STOXX. A total of 17 and 11 companies classified under the utility sector qualified for inclusion in these indices, respectively. We are one of the few German companies to have been listed in this family of indices without interruption since its inception in 1999.

Our transparent communications are also well received. We placed second in an evaluation of German sustainability reports supported by the German Sustainable Development Council, which was established by the German government. The study was conducted by the German Institute for Ecological Economy Research (IÖW) and the future e.V. company association. The reports of Germany's 150 largest companies were evaluated.

Responsibility Statement

3.0

To the best of our knowledge, and in accordance with the applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the Group review of operations includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group.

Essen, 13 February 2008

The Executive Board

Großmann Bonekamp Fitting Jobs Pohlig

Consolidated Financial Statements

4.0

4.1 Income Statement[1]

€ million	Note	2007	2006
Revenue (including natural gas tax/electricity tax)	(1)	**42,507**	**42,554**
Natural gas tax/electricity tax	(1)	1,454	1,385
Revenue		**41,053**	**41,169**
Changes in finished goods and work in progress		47	86
Other own work capitalized		81	134
Other operating income	(2)	1,232	1,687
Cost of materials	(3)	26,533	27,123
Staff costs	(4)	3,964	4,620
Depreciation, amortization, and impairment losses	(5)	2,257	2,265
of which: impairment losses on goodwill			(6)
Other operating expenses	(6)	3,885	4,507
Income from operating activities of continuing operations		**5,774**	**4,561**
Income from investments accounted for using the equity method	(7)	447	409
Other income from investments	(7)	150	381
Financial income	(8)	3,206	2,982
Finance costs	(8)	4,344	4,796
Income from continuing operations before tax		**5,233**	**3,537**
Taxes on income	(9)	2,076	966
Income from continuing operations		**3,157**	**2,571**
Income from discontinued operations		-274	1,442
Income		**2,883**	**4,013**
Minority interest		224	166
Net income/income attributable to RWE AG shareholders		**2,659**	**3,847**
Basic and diluted earnings per common and preferred share in €	(29)	**4.73**	**6.84**
of which: from continuing operations in €		(5.22)	(4.28)
of which: from discontinued operations in €		(-0.49)	(2.56)

1 Prior-year figures adjusted.

4.2 Balance Sheet

Assets € million	Note	12/31/07	12/31/06
Non-current assets			
Intangible assets	(10)	11,882	14,901
Property, plant and equipment	(11)	20,038	26,034
Investment property	(12)	153	225
Investments accounted for using the equity method	(13)	2,421	2,271
Other non-current financial assets	(14)	1,011	1,684
Financial receivables	(15)	1,338	1,537
Other receivables and other assets	(16)	1,693	1,093
Income tax assets	(17)	588	636
Deferred taxes	(18)	2,456	3,618
		41,580	**51,999**
Current assets			
Inventories	(19)	2,352	2,226
Financial receivables	(15)	1,702	2,945
Trade accounts receivable	(20)	8,816	8,876
Other receivables and other assets	(16)	7,534	7,673
Income tax assets		257	154
Marketable securities	(21)	10,858	16,788
Cash and cash equivalents	(22)	1,922	2,794
Assets held for sale		8,610	
		42,051	**41,456**
		83,631	**93,455**

Equity and Liabilities € million	Note	12/31/07	12/31/06
Equity	(23)		
RWE Group interest		14,131	13,439
Minority interest		787	672
		14,918	**14,111**
Non-current liabilities			
Provisions	(25)	21,212	28,632
Financial liabilities[1]	(26)	10,046	15,672
Other liabilities	(28)	3,584	5,021
Deferred taxes	(18)	1,928	3,077
		36,770	**52,402**
Current liabilities			
Provisions	(25)	5,713	5,434
Financial liabilities	(26)	3,239	3,710
Trade accounts payable	(27)	8,054	8,148
Income tax liabilities		93	123
Other liabilities	(28)	8,969	9,527
Liabilities held for sale		5,875	
		31,943	**26,942**
		83,631	**93,455**

1 Of which interest-bearing: €9,886 million (previous year: €15,233 million).

4.3 Cash Flow Statement

€ million	Note (33)	2007	2006
Income		2,883	4,013
Depreciation, amortization, impairment losses, write-backs		2,512	3,025
Changes in provisions		438	1,300
Changes in deferred taxes		656	293
Income from disposal of non-current assets and marketable securities		-631	-1,368
Other non-cash income/expenses		449	54
Changes in working capital		-222	-534
Cash flows from operating activities		**6,085**	**6,783**
Intangible assets/property, plant and equipment/investment property			
Capital expenditure		-4,065	-4,494
Proceeds from disposal of assets		112	322
Acquisitions and investments			
Capital expenditure		-155	-234
Proceeds from disposal of assets/divestitures		765	7,532
Changes in marketable securities and cash investments		-1,140	-5,597
Cash flows from investing activities		**-4,483**	**-2,471**
Net change in equity incl. minority interest		-14	-9
Dividends paid to RWE AG shareholders and minority interests		-2,199	-1,208
Issuance of financial debt		5,577	7,526
Repayment of financial debt		-5,822	-9,257
Cash flows from financing activities		**-2,458**	**-2,948**
Net cash change in cash and cash equivalents		-856	1,364
Effects of changes in foreign exchange rates and other changes in value on cash and cash equivalents		-16	-1
Net change in cash and cash equivalents		**-872**	**1,363**
Cash and cash equivalents at beginning of the reporting period		2,794	1,431
Cash and cash equivalents at end of the reporting period		**1,922**	**2,794**

4.4 Statement of Changes in Equity

Note (23) € million	Subscribed capital of RWE AG	Additional paid-in capital of RWE AG	Retained earnings and distributable profit	Accumulated other comprehensive income		**RWE Group interest**	Minority interest	**Total**
				Currency translation adjustments	Fair value measurement of financial instruments			
Balance at 01/01/06	**1,440**	**1,288**	**7,714**	**156**	**833**	**11,431**	**926**	**12,357**
Repayment of equity							-9	-9
Dividends paid[1]			-984			-984	-136	-1,120
Other comprehensive income				64	-899	-835	51	-784
Income			3,847			3,847	166	4,013
Total comprehensive income			3,847	64	-899	3,012	217	3,229
Other changes			-20			-20	-326	-346
Balance at 12/31/06	**1,440**	**1,288**	**10,557**	**220**	**-66**	**13,439**	**672**	**14,111**
Repayment of equity							-14	-14
Dividends paid[1]			-1,968			-1,968	-145	-2,113
Other comprehensive income				57	-91	-34	-11	-45
Income			2,659			2,659	224	2,883
Total comprehensive income			2,659	57	-91	2,625	213	2,838
Other changes			35			35	61	96
Balance at 12/31/07	**1,440**	**1,288**	**11,283**	**277**	**-157**	**14,131**	**787**	**14,918**

1 Due to the reclassification of minority interests to other liabilities as per IAS 32, the total dividends paid do not correspond to the dividends paid to RWE AG shareholders and minority interests as reported in the cash flow statement.

4.5 Notes

Basis of presentation

The consolidated financial statements for the period ended December 31, 2007 have been prepared in accordance with the International Financial Reporting Standards (IFRSs) applicable in the EU, as well as in accordance with the supplementary accounting regulations applicable pursuant to Sec. 315a, Para. 1 of the German Commercial Code (HGB). The previous year's figures have been calculated according to the same principles. The consolidated financial statements also comply with the IFRSs effective up to the balance-sheet date. Additionally, RWE is voluntarily applying IFRS 8 "Operating Segments" for the first time in this reporting period.

Changes in equity have been disclosed in addition to the income statement, the balance sheet and the cash flow statement. The notes to the financial statements also include segment reporting.

Several balance sheet and income statement items have been combined in order to improve clarity. These items are stated and explained separately in the notes to the financial statements. The income statement is structured according to the nature of expense method.

The consolidated financial statements have been prepared in euros. Unless specified otherwise, all amounts are stated in millions of euros (€ million).

These consolidated financial statements were prepared for the 2007 fiscal year (January 1 to December 31).

The Executive Board of RWE AG is responsible for the completeness and accuracy of the consolidated financial statements and the review of operations of the Group, which has been combined with the review of operations of RWE AG.

Internal control systems, the use of uniform directives throughout the Group, and our programmes for basic and advanced staff training ensure that the consolidated financial statements and combined review of operations are adequately prepared. Compliance with legal regulations and the internal guidelines as well as the reliability and viability of the control systems are continuously monitored throughout the Group.

In line with the requirements of the German Corporate Control and Transparency Act (KonTraG), the Group's risk management system enables the Executive Board to identify potential risks at an early stage and initiate countermeasures, if necessary.

The consolidated financial statements, the combined review of operations and the report of the independent auditors are discussed in detail by the Audit Committee and at the Supervisory Board's meeting on financial statements with the independent auditors present. The results of the Supervisory Board's examination are presented in the report of the Supervisory Board (pages 113 to 117 of this annual report).

Scope of Consolidation

In addition to RWE AG, the consolidated financial statements contain all material German and foreign companies which RWE controls directly or indirectly. Principal associates and joint ventures are accounted for using the equity method.

Investments in subsidiaries, joint ventures or associates which are of secondary importance from a Group perspective are accounted for in accordance with IAS 39. Subsidiaries which are not included in the scope of consolidation account for less than 1% of the Group's revenue, income and debt. Subsidiaries with negative income or equity are generally fully consolidated.

A collective listing of the Group's investments in accordance with Sec. 313, Para. 2, Nos. 1 to 4 and Para. 3 of the German Commercial Code (HGB) will be published in the electronic Federal Gazette (Bundesanzeiger). Material consolidated investments, investments accounted for using the equity method, and other investments are listed on pages 205 to 207 of this annual report.

Seven companies domiciled in Germany and 32 companies domiciled outside of Germany were consolidated for the first time in the year under review. Twelve companies, six of which are headquartered outside of Germany, are no longer included in the scope of consolidation; two companies based in Germany were merged. Seventy-two companies outside of Germany were deconsolidated due to classification as discontinued operations. Four investments, which had been accounted for using the equity method in the previous year, including one outside of Germany, were sold. Three companies outside of Germany are no longer reported as investments accounted for using the equity method due to classification as discontinued operations. First-time consolidation and deconsolidation generally take place when control is transferred.

Scope of consolidation	Germany 12/31/07	Foreign countries 12/31/07	Total 12/31/07	Total 12/31/06
Fully consolidated companies	140	150	290	337
Investments accounted for using the equity method	68	21	89	96

A total of €19 million was used to acquire stakes in companies which were consolidated for the first time (previous year: €0 million).

Discontinued operations. The sale of American Water Works Company Inc., Wilmington/Delaware, USA, was initiated in fiscal 2007. As a result, the companies previously disclosed in the Water Division are reported as discontinued operations in these statements. In accordance with IFRS 5, the prior-year figures in the income statement have been adjusted; the prior-year figures in the balance sheet and cash flow statement, however, have not been adjusted. American Water is still included in the roll-forward presentations of balance-sheet items and in the cash flow statement.

Key figures on the activities of American Water are presented in the following tables:

Key figures for American Water € million	12/31/07	12/31/06
Non-current assets	8,281	9,704
Current assets	329	356
Non-current liabilities	5,188	4,556
Current liabilities	687	1,296

€ million	2007	2006
Revenue	1,601	1,702
Expenses/income	-1,382	-1,582
Ordinary income from discontinued operations before tax	219	120
Taxes on income	-64	-16
Net income	155	104
Fair value adjustments	-429	
Income from discontinued operations	-274	104

€ million	2007	2006
Cash flows from operating activities	526	498
Cash flows from investing activities	-634	-521
Cash flows from financing activities	58	101

In the fourth quarter of fiscal 2007, an impairment test was performed for the cash-generating unit American Water. This test was performed on the basis of the fair value less expected costs to sell and resulted in a write-down of €429 million.

RWE Thames Water plc, which was sold as per contract dated October 16, 2006, was reported as a discontinued operation in the previous year's statements.

Key figures for RWE Thames Water are presented in the following tables:

Key figures for RWE Thames Water € million	2006
Revenue	2.278
Expenses/income	-1,806
Ordinary income from discontinued operations before tax	472
Taxes on income	-142
Net income	330
Income from the disposal	991
Income from discontinued operations	1,321

€ million	2006
Cash flows from operating activities	1,050
Cash flows from investing activities	-381
Cash flows from financing activities	139

Closing of the sale of RWE Umwelt to Remondis in 2005 resulted in supplementary payments amounting to €17 million after taxes in the following year, which were reported as income from discontinued operations in 2006.

With regard to subsidiaries and investments accounted for using the equity method, the following significant share disposals occurred during the year under review:

Subsidiaries:
- Obragas Net N.V., Netherlands
- BV Netbeheer Haarlemmermeer, Netherlands
- rhenag Rheinische Energie AG, Cologne, Germany, shareholding reduced by 25.1% to 74.9%

Investments accounted for using the equity method:
- Überlandwerk Groß-Gerau GmbH

Above and beyond this, the 30.2% stake in RAG AG reported under other investments was sold as per contract dated August 7, 2007. Transfer of the shares became legally effective as of November 30, 2007.

On balance, €135 million in non-current assets (including deferred taxes), €57 million in current assets (excluding cash and cash equivalents), €21 million in cash and cash equivalents and €156 million in non-current and current liabilities were derecognized as a result of the acquisition or disposal of consolidated enterprises.

The total selling price of the divested subsidiaries amounted to €446 million (previous year: €7,752 million), which was paid in cash or cash equivalents.

Effects of changes in the scope of consolidation have been stated in the notes insofar as they are of particular importance.

Consolidation principles

The financial statements of German and foreign companies included in the scope of consolidation are prepared using uniform accounting policies. On principle, subsidiaries with a different balance-sheet date prepare interim financial statements as of the Group's balance-sheet date.

Business combinations are reported according to the purchase method. Pursuant to this method, capital consolidation takes place by offsetting the purchase price against the acquired subsidiaries' revalued prorated net assets at the time of acquisition. Subsidiaries' identifiable assets, liabilities and contingent liabilities are measured at full fair value, regardless of the amount of the minority interest. Intangible assets are reported separately from goodwill if they are separable from the company or if they stem from a contractual or other right. In accordance with IFRS 3, no new restructuring provisions are recognized within the scope of the purchase price allocation. Acquisition costs not allocated to assets, liabilities, or contingent liabilities are capitalized as goodwill. Negative goodwill from first-time consolidation is included in income.

Capitalized goodwill is not amortized: it is tested for impairment once every year, or more frequently if there are indications of impairment. In deconsolidation, residual carrying amounts of capitalized goodwill are taken into account when calculating income from disposals.

Expenses and income as well as receivables and payables between consolidated companies are eliminated. Intragroup profits and losses are eliminated.

These consolidation principles also apply to investments accounted for using the equity method. In relation to these investments, goodwill is not reported separately: it is included in the recognized value of the investment. Such goodwill is not amortized either. If necessary, impairment losses on the equity value are reported under income from investments accounted for using the equity method. The financial statements of investments accounted for using the equity method are also prepared using uniform accounting policies.

Foreign currency translation

In their individual financial statements, the companies measure non-monetary foreign currency transactions at the balance-sheet date using the exchange rate in effect on the date they were initially recognized. Monetary items are converted using the exchange rate valid on the balance-sheet date. Exchange rate gains and losses from the measurement of monetary balance-sheet items in foreign currency occurring up to the balance-sheet date are recognized in the income statement under other operating expenses or income.

Functional foreign currency translation is applied when converting foreign companies' financial statements. As the principal foreign enterprises included in the consolidated financial statements conduct their business activities independently in their national currencies, the balance-sheet items of all foreign companies are translated into euros in the consolidated financial statements using the average exchange rate prevailing on the balance-sheet date. Goodwill is translated as an asset of the economically autonomous foreign entity at the exchange rate in effect on the balance-sheet date. Differences to previous-year translations are reported in other comprehensive income without an effect on income. Expense and income items are translated using annual average exchange rates. Annual financial statements of Group companies based in a country with hyperinflation are translated according to IAS 29. No material entities were headquartered in a country with hyperinflation in the fiscal year or previous year. When translating the adjusted equity of foreign companies accounted for using the equity method, the same procedure is followed.

The following exchange rates (among others) were used as a basis for foreign currency translations:

Exchange rates	Average		Year-end	
in €	2007	2006	12/31/07	12/31/06
1 US dollar	0.72	0.79	0.68	0.76
1 British pound	1.46	1.47	1.36	1.49
100 Czech korunas	3.61	3.54	3.76	3.64
100 Hungarian forints	0.40	0.38	0.39	0.40
1 Polish zloty	0.26	0.26	0.28	0.26

Accounting policies

Intangible assets are accounted for at amortized cost. With the exception of goodwill, all intangible assets have finite useful lives and are thus amortized using the straight-line method. Software for commercial and technical applications is amortized over three to five years. Easement agreements in the electricity and gas business, and other easement rights, generally have useful lives of up to 20 years. Concessions in the water business have terms of up to 50 years. Capitalized customer relations are amortized over a useful life of ten years. Useful lives and methods of amortization are reviewed on an annual basis.

Goodwill is not amortized; instead it is subjected to an impairment test once every year, or more frequently if there are indications of impairment.

Development costs are capitalized if a newly developed product or process can be clearly defined, is technically feasible and it is the company's intention to either use the product or process itself or market it. Furthermore, asset recognition requires that there be a sufficient level of certainty that the development costs will lead to future cash inflows. Capitalized development costs are amortized over the time period during which the products are expected to be sold. Research expenditures are recognized as expenses in the period in which they are incurred.

An impairment loss is recognized for an intangible asset, if the recoverable amount of the asset is less than its carrying amount. If the asset is part of a cash-generating unit (smallest identifiable group of assets which generates cash inflows that are largely independent of cash inflows from other assets or groups of assets), the impairment loss is calculated based on the recoverable amount of this unit. If this results in the carrying amount of a cash-generating unit to which goodwill was allocated exceeding the recoverable amount, the allocated goodwill is initially written down by the difference. Impairment losses which must be recognized in addition to this are taken into account by reducing the carrying amount of the other assets of the cash-generating unit on a prorated basis. If the reason for an impairment loss recognized in prior years has ceased to exist, a write-back is performed, whereby the increased carrying amount resulting from the write-back may not exceed the amortized cost. Impairment losses on goodwill are not reversed.

Property, plant and equipment is stated at depreciated cost. The borrowing cost is not capitalized as part of the cost. If necessary, the cost of property, plant and equipment may contain the estimated expenses for the decommissioning of plants or site restoration. Maintenance and repair costs are recognized as expenses.

Exploratory wells are accounted for at cost, according to the successful efforts method, i.e. expenses for exploration activities are only capitalized for successful projects. For example, only wells which are related to the discovery of crude oil or natural gas may be capitalized. Seismology and geology expenditures are recognized as expenses. Based on application of the unit-of-production method, capitalized exploration assets are not depreciated or amortized during the exploration phase; depreciation and amortization commences when production begins. Exploration assets are tested for impairment as soon as the technical feasibility and economic viability of production can be proven, or facts and information indicate that the carrying value exceeds the recoverable amount.

With the exception of land and leasehold rights, as a rule, property, plant and equipment is depreciated using the straight-line method, unless in exceptional cases another depreciation method is better suited to the usage pattern. The depreciation of typical property, plant and equipment is calculated according to the following useful lives, which apply throughout the Group:

Useful life in years	
Buildings	12 - 80
Technical plants	
Thermal power plants	15 - 20
Electricity grids	20 - 35
Water main networks	20 - 80
Gas and water storage facilities	20 - 100
Gas distribution facilities	14 - 20
Mining facilities	4 - 25
Mining developments	33 - 35
Wells owned by RWE Dea	up to 27

Property, plant and equipment held under a finance lease is capitalized at the lower of the fair value of the leased asset or the present value of the lease payments, and is depreciated using the straight-line method over its expected useful life or the lease term, whichever is shorter.

Impairment losses for plant, property and equipment are recognized according to the principles described for intangible assets. If the reason for an impairment loss recognized in prior years has ceased to exist, a write-back is performed, whereby the increased carrying amount resulting from the write-back may not exceed the depreciated cost.

Investment property is all real property held to earn rental income or for long-term capital appreciation rather than for use in production or for administrative purposes. This property is measured at depreciated cost. Transaction costs are also included in the initial measurement. Depreciable investment property is depreciated over 12 to 80 years using the straight-line method. Fair values of investment property are stated in the Notes under (12) and are determined using internationally accepted valuation methods such as the discounted cash flow method or are derived from the current market prices of comparable real estate.

Impairment losses for investment property are recognized according to the principles described for intangible assets. If the reason for an impairment loss recognized in prior years has ceased to exist, a write-back is performed, whereby the increased carrying amount resulting from the write-back may not exceed the depreciated cost.

Investments accounted for using the equity method are initially accounted for at cost and thereafter based on the carrying amount of their prorated net assets. The carrying amounts are increased or reduced annually by the prorated profits or losses, the dividends distributed and the other changes in equity. Goodwill is not reported separately: it is included in the recognized value of the investment. Goodwill is not amortized. An impairment loss is recognized for investments accounted for using the equity method, if the recoverable amount is less than the carrying amount.

Other financial assets are comprised of shares in non-consolidated subsidiaries and in joint ventures/associates not accounted for using the equity method, as well as other investments and non-current marketable securities; these assets are nearly exclusively shown in the category “available for sale”. Financial instruments which are neither loans or receivables, nor held to maturity and are not measured at fair value through profit or loss are allocated to this category. Initially and in the following periods, they are measured at fair value as long as such can be determined reliably. They are initially valued on their settlement date. Unrealized gains and losses are stated as other comprehensive income, with due consideration of any deferred taxes.

Gains or losses are recognized in the income statement at the time of sale. If there are objective, material indications of a reduction in the value of an asset, an impairment loss is recognized with an effect on income. Indications of impairment can include significant financial difficulties of the debtor, default or delinquency on payments of interest or principal, or the disappearance of an active market for a financial asset as a result of problems in the financial system.

Receivables are comprised of ***financial receivables, trade accounts receivable*** and ***other receivables***. With the exception of financial derivatives, ***receivables and other assets*** are stated at amortized cost. Allowances for doubtful accounts are based on the actual default risk. As a rule, the amounts of receivables are corrected through the use of an allowance account, in accordance with internal Group guidelines. Prepayments received from customers for consumption which is yet to be metered and billed are netted out against trade accounts receivable of the utilities.

Loans reported under financial receivables are stated at amortized cost. Loans with interest rates common in the market are shown on the balance sheet at nominal value; as a rule, non-interest or low-interest loans are disclosed at their present value discounted using an interest rate that is commensurate with the risks involved.

CO_2 emission allowances are accounted for as intangible assets and reported under other assets. They are stated at cost and are not amortized.

Deferred taxes result from temporary differences in the carrying amount in the separate IFRS financial statements and the tax base, and from consolidation procedures. Deferred tax assets also include tax reduction claims resulting from the expected utilization of existing loss carryforwards in subsequent years. Deferred taxes are capitalized when their realization is guaranteed with sufficient certainty. The amount of deferred taxes is assessed based on the tax rates that are applicable or expected in the individual countries at the time of realization, with due consideration of the tax regulations valid or adopted as of the balance-sheet date. The tax rate used to calculate deferred taxes in Germany is 30.9% (previous year: 39.4%). This is derived from the 15% corporate tax rate effective from January 1, 2008 (previous year: 25%), the unchanged 5.5% solidarity surcharge, and the Group's average local trade tax rate in Germany. Deferred tax assets and deferred tax liabilities are netted out for each company and/or tax group.

Inventories include all assets which are held for sale in the ordinary course of business (finished goods and goods for resale), which are in the process of production (work in progress – goods and services) or which are consumed in the production process or in the rendering of services (raw materials including nuclear fuel assemblies and excavated earth for lignite mining).

Inventories are carried at the lower of cost or the net realizable value. Production costs reflect the full costs directly related to production and are determined based on the normal capacity. Specifically, in addition to directly allocable costs, production costs include adequate portions of required materials and production overheads, including production-related depreciation. The borrowing cost is not capitalized as part of the cost. Assessment is generally based on average values. The usage of excavated earth for lignite mining is calculated using the FIFO method.

If the net realizable value of inventories written down in earlier periods has increased, the resulting reversal of the write-down is recognized as a reduction of the cost of materials.

Nuclear fuel assemblies are stated at depreciated cost. Depreciation is determined by operation and capacity, based on consumption and the reactor's useful life.

Securities classified as current ***marketable securities*** essentially consist of marketable securities held in special funds as well as fixed-interest securities which have a maturity of more than three months and less than one year from the date of acquisition. All of these securities are classified as "available for sale" and are stated at fair value. The transaction costs directly associated with the acquisition of the financial asset are included in the initial measurement. These securities are initially measured on their settlement date. Unrealized gains and losses are included in other comprehensive income, with due consideration of any deferred taxes. Gains or losses are recognized in the income statement at the time of sale. If there are objective, material indications of a reduction in the value of an asset, an impairment loss is recognized with an effect on income.

Financial assets are derecognized when the contractual rights to cash flows from the asset expire or the entity transfers the financial asset. The latter applies when substantially all the risks and rewards of ownership of the asset are transferred, or the entity no longer has control of the asset.

Cash and cash equivalents consist of cash on hand, demand deposits and current fixed-interest securities with a maturity of three months or less from the date of acquisition.

Assets are stated under "***Assets held for sale***" if they can be sold in their present condition and their sale is highly probable. Such assets may be certain non-current assets, asset groups ("disposal groups") or operations ("discontinued operations"). Liabilities intended to be sold in a transaction together with assets are a part of a disposal group or discontinued operations, and are reported separately under "***Liabilities held for sale***".

Non-current assets held for sale are no longer depreciated or amortized; they are recognized at fair value less costs to sell, as long as this is lower than the carrying amount.

Gains or losses on the valuation of specific assets held for sale and of disposal groups are stated under income from continuing operations until final completion of the sale.

Gains or losses on the valuation of discontinued operations at fair value less costs to sell are reported under income from discontinued operations. The same procedure is applied for profits or losses from operating activities or from the sale of such operations.

The groupwide stock option plans are accounted for as cash-settled ***share-based payment***. At each reporting date, a provision is recognized in the amount of the prorated fair value of the payment obligation; changes in the fair value are recognized with an effect on income. The fair value of options is determined using generally accepted valuation methodologies.

Provisions are recognized for all legal or constructive obligations to third parties which exist on the balance-sheet date and relate to past events, and with regard to which it is probable that an outflow of resources will be required, and the amount of which can be reliably estimated. Provisions are carried at the individually most likely outcome and are not offset against reimbursement claims. Provisions based on a large number of similar events are stated at the expected amounts of the possible outcomes.

All non-current provisions are recognized at the most likely outcome that is discounted as of the balance-sheet date. The settlement amount also includes the cost increases to be taken into account as of the balance-sheet date.

If necessary, the cost of property, plant and equipment may contain the estimated expenses for the decommissioning of plants or site restoration, for which decommissioning, restoration and similar provisions are recognized. In respect of these provisions, changes in the estimated timing or amount of the payments and changes in the discount rate are taken into account at the same amount in measuring the existing provision as well as the respective asset. If the decrease in the provision exceeds the carrying amount of the underlying asset, the excess is recognized immediately through profit or loss. Releases of provisions are credited to the expense account on which the provision was originally recognized.

Provisions for pensions and similar obligations are recognized for defined benefit plans. These are obligations of the company to pay future and ongoing post-employment benefits to entitled current and former employees and their surviving dependents. In particular, the obligations refer to retirement pensions in the form of both basic and supplementary benefits. Individual commitments are based on the differing industry- and country-specific benefit arrangements and are generally calculated according to the employees' length of service and compensation. As benefits, the obligations of US Group enterprises for their employees' post-retirement medical expenses are also disclosed under provisions for pensions and similar obligations.

Provisions for defined benefit plans are measured according to the projected unit credit method. This benefit/years-of-service method not only takes into account the pension benefits and benefit entitlements known as of the balance-sheet date, but also increases in salaries and pension benefits to be expected in the future. The calculation is based on actuarial reports, taking into account appropriate biometric parameters. The provision is reduced by the amount of the plan assets. The service cost is disclosed in staff costs, and the interest cost and expected return on plan assets are reported in the financial result.

Actuarial gains and losses exceeding 10% of the greater of the benefit obligations or the fair value of plan assets are amortized over the anticipated average remaining working lives of the entitled employees, with an effect on income ('corridor method').

In the case of defined contribution plans, the enterprise's obligation is limited to the amount it contributes to the plan. The contributions to the plan are recognized as expenses and disclosed under staff costs.

Waste management provisions in the nuclear energy sector are based on obligations under public law, in particular the German Atomic Energy Act, and on restrictions stipulated in operating licenses. These provisions are measured using estimates, which are based on and defined in contracts, on information from internal and external specialists and expert opinions, as well as on data from the German Federal Office for Radiation Protection (BfS).

Provisions for mining damage are recognized to cover land recultivation obligations and obligations to restore mining damage that has already occurred or been caused. Such risks and obligations are those that exist as of the balance-sheet date or are identifiable when the balance sheet is being prepared. They must be recognized due to obligations under public law, such as the German Federal Mining Act, and formulated, above all, in operating schedules and water law permits. Provisions are generally recognized based on the increase in the obligation, e.g. in line with lignite production. Such provisions are measured at full expected cost or according to estimated compensation payments.

Furthermore, provisions are made owing to obligations under public law to dismantle production facilities and fill wells. The amount of these provisions is determined on the basis of total cost estimates, which reflect past experience and the comparative rates determined by the German Association of Oil and Natural Gas Production Industry. Similar assumptions for foreign subsidiaries are also taken into account.

A provision is recognized to cover the obligation to return CO_2 emission allowances to the competent authorities; this provision is measured at the book value of the CO_2 allowances capitalized for this purpose. If a portion of the obligation is not covered with the available allowances, the provision for this portion is measured using the market price of the allowances on the reporting date.

Liabilities consist of ***financial liabilities, trade accounts payable*** and ***other liabilities.*** Upon initial recognition, liabilities are stated at fair value including transaction costs. In the periods thereafter, liabilities (except for financial derivatives) are carried at amortized cost. Liabilities from finance lease agreements are measured at the lower of fair value of the leased asset or present value of minimum lease payments.

Deferred income and prepayments from customers are recognized as liabilities under other liabilities. Deferred income includes advances and contributions in aid of construction and building connection that are carried as liabilities by the utilities and which are generally amortized and included in income over the term of the corresponding asset. Moreover, this item also generally includes taxable and non-taxable government grants for capital expenditure on non-current assets, which are recognized as other operating income in line with the assets' depreciation.

Certain minority interests are also presented under other liabilities. Specifically, this pertains to purchase price obligations from put options and forward purchases of minority interests that are recognized in accordance with IAS 32.

Derivative financial instruments are recognized as assets or liabilities. All derivative financial instruments are stated at fair value regardless of their purpose. Changes in the fair value are recognized with an effect on income, unless the instruments are used for hedging purposes. In such cases, recognition of changes in the fair value depends on the type of hedging transaction.

Fair value hedges are used to hedge the risk of a change in the fair value of an asset or liability carried on the balance sheet. Hedges of unrecognized firm commitments are also recognized as fair value hedges. For fair value hedges, changes in the fair value of the hedging instrument are stated in the income statement, analogously to the changes in the fair value of the respective underlying transactions, i.e. gains and losses from the fair valuation of the hedging instrument are allocated to the same line items of the income statement as those of the related hedged item. In this regard, changes in the fair value of the underlying transaction must pertain to the hedged portion of the overall risk. In the event that unrecognized firm commitments are hedged, changes in the fair value of the firm commitments with regard to the hedged risk result in the recognition of an asset or liability with an effect on income.

Cash flow hedges are used to hedge the risk of variability in cash flows related to an asset or liability carried on the balance sheet or related to a highly probable forecast transaction. If a cash flow hedge exists, unrealized gains and losses from the hedging instrument are initially stated as other comprehensive income. Such gains or losses are disclosed in the income statement when the hedged underlying transaction has an effect on income. If forecast transactions are hedged and such transactions lead to the recognition of a financial asset or financial liability in subsequent periods, pursuant to IAS 39 the amounts that were recognized in equity until this point in time are recognized in the income statement in the period during which the asset or liability affects the income statement. If the transaction results in the recognition of non-financial assets or liabilities, the amounts recognized in equity without an effect on income are included in the initial cost of the asset or liability.

The purpose of hedges of a net investment in a foreign entity is to hedge the currency risk from investments with foreign functional currencies. Unrealized gains and losses from hedges are recognized in other comprehensive income until the investment is sold.

The conditions for hedge accounting are stipulated in IAS 39. In particular, the hedging relationship must be documented in detail and be effective, i.e. the changes in the fair value of the hedging instrument must be within 80 to 125%, both prospectively and retrospectively, of the opposite change in the fair value of the hedged item. Only the effective portion of a hedge is recognized in accordance with these rules. The ineffective portion of a hedge is recognized immediately in the income statement with an effect on income.

Contracts that were entered into and continue to be held for the purpose of receipt or delivery of non-financial items in accordance with the company's expected purchase, sale or usage requirements (own-use contracts) are not accounted for as derivative financial instruments, but rather as executory contracts. If the contracts contain embedded derivatives, the derivatives are accounted separately from the host contract, if the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host contract. Written options to buy or sell a non-financial item which can be settled in cash are not own-use contracts.

Contingent liabilities are possible obligations to third parties or existing obligations, which are not recognized because it is not probable that an outflow of economic benefits will be required to settle the obligations or the amount of which cannot be measured reliably. Contingent liabilities are not recognized on the balance sheet, unless they are assumed within the framework of a business combination. The amounts disclosed in the notes correspond to the exposure at the balance-sheet date.

Management judgments in the application of accounting policies. Management judgments are required in the application of accounting policies. In particular, this pertains to the following items:

- With regard to certain contracts a decision must be made as to whether they are to be treated as derivatives or as so-called own-use contracts, and be accounted for as executory contracts.
- Financial assets must be allocated to the categories "held to maturity investments", "loans and receivables", "financial assets available for sale", and "financial assets at fair value through profit or loss".
- With regard to provisions for pensions and similar liabilities, there are various options for the recognition of actuarial gains and losses.
- With regard to assets held for sale, it must be determined if they can be sold in their current condition and if the sale of such is highly probable. If both conditions apply, the assets and any related liabilities must be reported and measured as "Assets held for sale" or "Liabilities held for sale", respectively.

The explanation of the accounting policies contains a description of the decisions taken by the RWE Group with regard to these items.

Management estimates and judgments. Preparation of consolidated financial statements pursuant to IFRS requires assumptions and estimates to be made, which have an impact on the recognized value of the assets and liabilities carried on the balance sheet, on income and expenses and on the disclosure of contingent liabilities.

Amongst other things, these assumptions and estimates relate to the accounting and measurement of provisions. With regard to pension provisions and similar obligations, the expected return on plan assets and the discount rate are very important estimates. In Germany, an increase or decrease of one percentage point in the discount rate would result in a reduction of €1,280 million or an increase of €1,706 million, respectively, in the present value of the obligations of our pension plans. For the Group companies in the UK, identical changes in the discount rate would reduce or increase pension obligations by €545 million or €668 million, respectively.

The impairment test for goodwill is based on certain assumptions pertaining to the future. Based on current knowledge, changes in these assumptions will not cause the carrying amounts of the cash-generating units to exceed the recoverable amounts, and thus will also not result in an adjustment of the carrying amounts in the next fiscal year. Due to the planned disposal of the North American water business, the valuation of this cash-generating unit is based on market-related data, and changes in such may have an impact on the carrying amount. In particular, the valuation depends on the equity market conditions prevailing at the time of recognition, the development of long-term interest rates on the capital market and the development of assets subject to regulation as well as the decisions of the local regulatory authorities.

Deferred tax assets are recognized when realization of future tax benefits becomes probable. Actual future income for tax purposes and hence the actual realizability of deferred tax assets may deviate from the estimation made when the deferred taxes are capitalized.

Further explanation of assumptions and estimates are presented in the notes to the individual items in the financial statements.

All assumptions and estimates are based on the circumstances and forecasts prevailing on the balance-sheet date. Furthermore, as of the balance-sheet date realistic assessments of overall economic conditions in the sectors and regions in which the Group conducts operations are taken into consideration with regard to the expected future development of business. Actual amounts may differ from the estimated amounts due to deviation between the assessments and the actual development of such overall conditions. In such cases, the assumptions, and, if necessary, the carrying amounts of the affected assets and liabilities are adjusted.

As of the date of preparation of the consolidated financial statements it is not presumed that there will be a material change in the assumptions and estimates. Therefore, from the current perspective there is no expectation of material adjustment to the carried amounts of the recognized assets and liabilities in the 2008 fiscal year.

Capital management. The broader framework for optimized capital management is determined by the strategic approach of the RWE Group, which is focused on increasing the value of our business over the long term, in the interests of our investors, employees and customers. RWE aims to achieve this goal by constantly improving its results through organic growth and higher efficiency. In doing so, it is necessary to balance the business and financial risks on the one hand with the financial flexibility required to reach the growth targets on the other. This balance is guaranteed by the strong financial profile which RWE has committed to.

One aspect of maintaining a strong financial profile is RWE's credit rating, which is influenced by a number of qualitative and quantitative factors. These include aspects such as market conditions, competition and the political framework, as well as indicators such as profitability and cash flow generation.

The review of operations contains the assessment of our current creditworthiness by the rating agencies Moody's and Standard & Poor's, both of which assign the fifth-best rating for RWE AG's long-term creditworthiness. Both rating agencies give the highest possible rating for RWE's short-term credit quality and the Commercial Paper Programme.

RWE AG is not subject to any capital requirements on the basis of its Articles of Incorporation.

Changes in accounting policies

The International Accounting Standards Board (IASB) has approved a number of changes to the existing International Financial Accounting Standards (IFRSs) and adopted several new IFRSs, which became effective as of January 1, 2007. The RWE Group is applying the following IFRSs in the reporting period for the first time:

IFRS 7 "Financial instruments: Disclosures" combines and expands disclosures of financial instruments previously required under IAS 32 and those previously required under IAS 30 only for banks and similar financial institutions. IFRS 7 is now effective across all industries. In connection with the publication of IFRS 7, IAS 1 was amended to add requirements for disclosures about capital management. With the exception of the additional information in the notes, the first-time application of IFRS 7 has no impact on the RWE Group's consolidated financial statements.

IFRIC 7 "Applying the Restatement Approach under IAS 29 'Financial Reporting in Hyperinflationary Economies'" clarifies certain issues related to the application of IAS 29 for cases in which the country, the currency of which is the functional currency of the reporting enterprise, becomes a hyperinflationary country. The first-time application of IFRIC 7 has no impact on the RWE Group's consolidated financial statements.

IFRIC 8 "Scope of IFRS 2" clarifies the applicability of IFRS 2 "Share-based Payment" to agreements, in which the reporting company makes share-based payments for apparently nil or inadequate consideration. The first-time application of IFRIC 8 has no impact on the RWE Group's consolidated financial statements.

IFRIC 9 "Reassessment of Embedded Derivatives" makes it clear that a contract must be assessed for embedded derivatives as per IAS 39 only upon inception or significant changes in the contract. The first-time application of IFRIC 9 has no impact on the RWE Group's consolidated financial statements.

IFRIC 10 "Interim Financial Reporting and Impairment" applies to the interaction of the regulations of IAS 34 on Interim Financial Reporting and the regulations of IAS 36 and IAS 39 on the reversal of impairment losses with regard to certain assets. The Interpretation makes it clear that impairments recognized in interim reports may not be reversed. The first-time application of IFRIC 10 has no impact on the RWE Group's consolidated financial statements.

Above and beyond this, RWE is voluntarily applying ***IFRS 8 "Operating Segments"***, which was adopted in November 2006, for the first time during the year under review. Pursuant to IFRS 8, segment reporting is to be prepared according to the "management approach". This means that the definition of segments and the disclosures for these segments are based on the information which is used internally by management in deciding how to allocate resources and in assessing the performance of the divisions. As of December 31, 2007, the first-time application of IFRS 8 had no impact on the definition of segments in the RWE Group; segment reporting is presented in the Notes under (32).

In the year under review, the variation margins, which were reported in previous years under collaterals for trading activities, were netted out against the market values of the underlying derivatives. These variation margins are used on a daily basis to pay or debit exchange counterparties for changes in the value of a future position on the European Energy Exchange (EEX), Leipzig, Germany, resulting from the difference between the previous day's price and the price on the current trading day.

Starting from January 1, 2008, in accordance with IAS 19.93A, actuarial gains and losses in the RWE Group will no longer be recognized in accordance with the 'corridor method', but entirely during the period in which they occur. Such gains or losses will be reported outside profit or loss, in a statement of recognized income and expenses in consolidated equity. This transition will result in a reduction of consolidated equity amounting to approximately €0.3 billion.

New accounting policies

The International Accounting Standards Board (IASB) and International Financial Reporting Interpretations Committee (IFRIC) have adopted further standards and interpretations, which were not yet mandatory in the 2007 financial year. These IFRSs can only be applied if they are endorsed by the EU, which is still pending in some cases.

Amendment of IFRS 2 (2008) "Vesting Conditions and Cancellations" clarifies the definition of vesting conditions in share-based payments and stipulates that all cancellations of share-based payments should receive identical accounting treatment, regardless of the party responsible for cancellation. Published on January 17, 2008, this amendment of IFRS 2 becomes effective for the first time for fiscal years starting on or after July 1, 2009. The impact of the first-time application of these amendments on the RWE Group's consolidated financial statements is currently being reviewed.

IFRS 3 (2008) "Business Combinations" contains amended regulations on the accounting of business combinations. In particular, these changes involve the scope of application and the treatment of successive share purchases and the introduction of an option allowing non-controlling interests to be measured at fair value or at the proportionate share of net assets. Depending on which option a company exercises, any goodwill is recognized in full or only in proportion to the majority owner's interest. IFRS 3 (2008), published on January 10, 2008, becomes effective for the first time for fiscal years starting on or after July 1, 2009. The impact of the first-time application of these amendments on the RWE Group's consolidated financial statements is currently being reviewed.

IAS 1 (2007) "Presentation of Financial Statements" contains new regulations on the presentation of financial statements. Above all, future non-owner changes in equity are to be strictly separated from owner changes in equity, and disclosure on other comprehensive income is to be extended. IAS 1 (2007) becomes effective for the first time for fiscal years starting on or after January 1, 2009. The first-time application of IAS 1 (2007) will result in changes in the presentation of the income statement and statement of changes in equity in RWE's consolidated financial statements.

IAS 23 (2007) "Borrowing Costs": By revising IAS 23, the IASB abolished the option for the treatment of borrowing costs directly incurred in connection with the acquisition, construction or production of qualified assets. In the future, these borrowing costs must be assigned to the asset's cost and capitalized. IAS 23 (2007) becomes effective for the first time for fiscal years starting on or after January 1, 2009. The impact of the application of the new rules on the RWE Group's consolidated financial statements is currently being reviewed.

IAS 27 (2008) "Consolidated and Separate Financial Statements": By revising IAS 27, the IASB changed the regulations on treatment of transactions between the non-controlling and controlling interests of a group and the treatment in the event of loss of control over a subsidiary. Transactions which result in the parent company changing its ownership interest in a subsidiary without a loss of control over the subsidiary are to be accounted for as equity transactions without an effect on profit or loss. Moreover, the standard regulates how deconsolidation gains are to be calculated and how residual ownership interest in the former subsidiary is to be measured. The revised version of IAS 27 was published on January 10, 2008 and must be applied for the first time for fiscal years starting on or after July 1, 2009. The impact of the application of the new rules on the RWE Group's consolidated financial statements is currently being reviewed.

IFRIC 11 "IFRS 2 – Group and Treasury Share Transactions" provides guidance on how to apply IFRS 2 to share-based payments involving a company's own equity instruments or equity instruments of a company from the same group. This Interpretation becomes effective for the first time for fiscal years starting on or after March 1, 2007. The first-time application of IFRIC 11 is not expected to have a material impact on the RWE Group's consolidated financial statements.

IFRIC 12 "Service Concession Arrangements" governs the accounting for arrangements in which a public agency concludes a contract with a private company for the supply of public services. In order to provide these services, the private company uses infrastructure which remains under public control. The private company is responsible for the construction, operation and maintenance of the infrastructure. This Interpretation becomes effective for the first time for fiscal years starting on or after January 1, 2008. The impact of the first-time application of IFRIC 12 on the RWE Group's consolidated financial statements is currently being reviewed.

IFRIC 13 "Customer Loyalty Programmes" addresses the accounting of revenue in connection with loyalty award credit programmes granted by manufacturers or service providers directly, or via third parties. This Interpretation becomes effective for the first time for fiscal years starting on or after July 1, 2008. The impact of the first-time application of IFRIC 13 on the RWE Group's consolidated financial statements is currently being reviewed.

IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" addresses detailed issues related to the accounting treatment of pension plans. This Interpretation becomes effective for the first time for fiscal years starting on or after January 1, 2008. The impact of the first-time application of IFRIC 14 on the RWE Group's consolidated financial statements is currently being reviewed.

Notes to the Income Statement

(1) Revenue (including natural gas tax/electricity tax)

Revenue is recorded when the risk stemming from a delivery or service has been transferred to the customer.

To improve the presentation of business development, RWE reports revenue generated by energy trading operations as net figures, reflecting realized gross margins. By contrast, electricity, gas, coal and oil transactions that are subject to physical settlement are stated as gross figures. Energy trading revenue is generated by RWE Trading. In fiscal 2007, gross revenue (including energy trading) amounted to €65,097 million (previous year: €70,213 million).

The segment reporting on pages 196 to 199 contains a breakdown of revenue (including natural gas tax/electricity tax) by division and geographical region. Deconsolidations and first-time consolidations reduced revenue by a net €806 million.

Natural gas tax/electricity tax are the taxes paid directly by Group companies.

(2) Other operating income

€ million	2007	2006
Release of provisions	230	260
Cost allocations/refunds	57	255
Disposal and write-back of current assets excluding marketable securities	43	249
Disposal of non-current assets including income from deconsolidation	353	191
Income from derivative financial instruments	148	107
Compensation for damage/insurance benefits	14	53
Rent and lease	32	34
Miscellaneous	355	538
	1,232	**1,687**

Income from the disposal of non-current financial assets and loans is disclosed under income from investments if it relates to investments; otherwise it is recorded as part of the financial result as is the income from the disposal of current marketable securities.

A decrease of €26 million in other operating income is attributable to changes in the scope of consolidation.

(3) Cost of materials

€ million	2007	2006
Cost of raw materials and of goods for resale	21,484	22,095
Cost of purchased services	5,049	5,028
	26,533	**27,123**

The cost of raw materials used also contains expenses for the use and disposal of spent nuclear fuel assemblies as well as €24 million (previous year: €119 million) in taxes paid for RWE Dea's foreign production companies.

Cost of materials in exploration activities amounted to €133 million in the reporting period (previous year: €100 million).

A total of €22,590 million in energy trading revenue (previous year: €27,659 million) was netted out against cost of materials. Changes in the scope of consolidation resulted in a decrease of €432 million in the cost of materials.

(4) Staff costs

€ million	2007	2006
Wages and salaries	3,277	3,909
Cost of social security, pensions and other benefits	687	711
	3,964	**4,620**

The cost of pension benefits was €30 million (previous year: -€22 million), consisting of €178 million in current service cost (previous year: €160 million), amortization of past service cost of -€161 million (previous year: -€199 million) and recognized actuarial losses with an effect on income in the amount of €13 million (previous year: €17 million).

Converted to full-time positions, the RWE Group's average personnel headcount (excluding American Water) totalled 63,054 (previous year: 65,910). Part-time and fixed-term employment relationships are included in accordance with the ratio of the part-time work or the duration of the employment to the annual employment time. In addition, on average the Group employed 2,591 trainees (previous year: 2,644).

A decrease of €268 million in staff costs is attributable to changes in the scope of consolidation.

(5) Depreciation, amortization, and impairment losses

Depreciation and impairment losses on property, plant and equipment amounted to €1,781 million (previous year: €1,750 million) and to €8 million (previous year: €21 million) on investment property. Intangible assets were written down by €468 million (previous year: €494 million), of which €327 million (previous year: €327 million) pertained to customer relationships in connection with acquisitions from prior financial years. Depreciation, amortization and impairment losses of €1 million (previous year: €22 million) were recognized on property, plant and equipment and intangible assets in exploration.

Impairment losses were recognized in the reporting period. These impairment losses amounted to €85 million (previous year: €102 million) on property, plant and equipment, and to €2 million (previous year: €4 million) on investment property. Impairment losses of €3 million (previous year: €3 million) were recorded on intangible assets (with the exception of goodwill); €0 million in impairment losses on goodwill were recognized in the year under review (previous year: €6 million).

A reduction of €25 million in depreciation, amortization and impairment losses resulted from changes in the scope of consolidation.

(6) Other operating expenses

€ million	2007	2006
Maintenance and renewal obligations	599	602
Additions to provisions	571	614
Concessions, licenses and other contractual obligations	483	525
Structural and adaptation measures	91	309
Legal and other consulting and data processing services	193	255
Disposal of current assets and decreases in values excluding inventories and marketable securities	327	287
Disposal of non-current assets including expenses from deconsolidation	49	283
Insurance, commissions, freight and similar distribution costs	199	203
General administration	189	202
Advertising	192	177
Expenses from derivative financial instruments	141	130
Lease payments for plant and grids as well as rents	94	103
Postage and monetary transactions	85	86
Fees and membership dues	80	82
Other taxes, primarily on property	24	47
Miscellaneous	568	602
	3,885	**4,507**

Exploration activities resulted in other operating expenses of €48 million (previous year: €32 million).

A decrease of €104 million in other operating expenses is attributable to changes in the scope of consolidation.

(7) Income from investments

Income from investments includes all income and expenses which have arisen in relation to operating investments. It is comprised of income from investments accounted for using the equity method and other income from investments.

Income from investments € million	2007	2006
Income from investments accounted for using the equity method	**447**	**409**
of which: amortization and impairment losses on investments accounted for using the equity method	(-3)	(-70)
Income from non-consolidated subsidiaries	14	12
of which: amortization and impairment losses on non-consolidated subsidiaries	(-2)	(-5)
Income from other investments	61	12
of which: impairment of shares in other investments	(-1)	(-42)
Income from the disposal of investments	40	331
Expenses from the disposal of investments	2	13
Income from loans to investments	47	36
Expenses from loans to investments	10	
Other		3
Other income from investments	**150**	**381**
	597	**790**

Income from investments includes impairment losses on other financial assets in the amount of €3 million (previous year: €47 million) and impairment losses on loans to investments amounting to €10 million (previous year: €0 million).

(8) Financial result

€ million	2007	2006
Interest and similar income	855	2,201
Other financial income	2,351	781
Financial income	**3,206**	**2,982**
Interest and similar expenses	1,334	2,710
Interest accretion to		
Provisions for pensions and similar obligations	149	504
Provisions for nuclear waste management as well as to mining provisions	548	529
Other provisions	74	103
Other finance costs	2,239	950
Finance costs	**4,344**	**4,796**
	-1,138	**-1,814**

The financial result breaks down into net interest, interest accretion to provisions and other financial income and other finance costs.

Net interest includes interest income from all interest-bearing securities and loans, expenses and income relating to marketable securities and all interest expenses. Net interest also includes shares in profit and dividends from non-current and current marketable securities.

Net interest € million	2007	2006
Interest and similar income	855	2,201
Interest and similar expenses	1,334	2,710
	-479	**-509**

Interest accretion to provisions contains the reversal allocable to the current year of the discounting of non-current provisions from the annual update of the present value calculation. This also includes income on plan assets for the coverage of pension obligations.

Net interest is composed of financial assets and liabilities, which are allocated to the following categories:

Interest result by category € million	2007	2006
Loans and receivables	479	1,802
Financial assets available for sale	376	399
Financial liabilities carried at (amortized) cost	-1,334	-2,710
	-479	**-509**

The financial result also contains all other financial income and finance costs which cannot be allocated to net interest or to interest accretion to provisions. Other financial income includes €572 million in gains realized from the disposal of marketable securities (previous year: €408 million). Other finance costs include write-downs of marketable securities due to decreases in their fair value in the amount of €42 million (previous year: €59 million) as well as €266 million (previous year: €172 million) in realized losses from the disposal of marketable securities.

(9) Taxes on income

€ million	2007	2006
Current taxes on income	1,455	713
Deferred taxes	621	253
	2,076	**966**

Current taxes on income contain €65 million in net tax income (previous year: expenses of €62 million) relating to prior periods.

Due to the German Corporate Tax Reform Act of 2008, the average comprehensive income tax rate for enterprises taxed in Germany will decline from 39.4% to 30.9% in fiscal 2008. The necessary recalculation of domestic deferred taxes resulted in an expense of €256 million in the year under review. Corporate tax rates will also be reduced in the UK and the Czech Republic next year. The resulting recalculation of deferred taxes led to non-recurrent tax income of €41 million and €25 million, respectively. In the previous year, an increase of €6 million in deferred taxes was recognized as an expense due to changes in tax rates.

Due to the utilization of tax loss carryforwards unrecognized in prior years, current taxes on income were reduced by €11 million (previous year: €2 million). Deferred tax expenses decreased by €26 million (previous year: €48 million), due to previously unrecognized tax loss carryforwards that are to be reassessed.

The income tax expense is derived from the theoretical tax expense. A tax rate of 39.4% was applied to income from continuing operations before tax, as in the previous year.

Tax reconciliation € million	2007	2006
Income from continuing operations before tax	**5,233**	**3,537**
Theoretical tax expense	**2,062**	**1,394**
Differences from foreign tax rates	-377	-150
Tax effects on		
Tax-free domestic dividend income	-118	-153
Tax-free foreign dividend income	-24	-41
Other tax-free income	-26	-1
Expenses not deductible for tax purposes	150	71
Impairment losses on goodwill from capital consolidation		2
Accounting for associates using the equity method (including impairment losses on associates' goodwill)	-57	5
Unutilizable loss carryforwards and/or utilization of unrecognized loss carryforwards and write-downs on loss carryforwards	34	-38
Income on the disposal of investments	-185	67
Changes in domestic tax rates	256	
Changes in foreign tax rates	-66	6
Other	427	-196
Effective tax expense	**2,076**	**966**
Effective tax rate in %	39.7	27.3

Notes to the Balance Sheet

(10) Intangible assets[1]

€ million	Development costs	Concessions, patent rights, licenses and similar rights	Customer relationships and similar assets	Goodwill	Pre-payments	Total
Cost						
Balance at 01/01/07	253	1,459	3,050	13,058	40	17,860
Additions/disposals due to changes in the scope of consolidation	-9	-48	9	-2,747	-34	-2,829
Additions	52	217	1		16	286
Transfers		11			-11	
Currency translation adjustments	-16	-25	-258	-597	-6	-902
Disposals	1	46				47
Balance at 12/31/07	279	1,568	2,802	9,714	5	14,368
Accumulated amortization/impairment losses						
Balance at 01/01/07	122	854	1,243	740		2,959
Additions/disposals due to changes in the scope of consolidation	4	-29		-657		-682
Amortization/impairment losses in the reporting period	41	102	327			470
Currency translation adjustments	-9	-9	-125	-77		-220
Disposals		41				41
Write-backs						
Balance at 12/31/07	158	877	1,445	6		2,486
Carrying amounts						
Balance at 12/31/07	121	691	1,357	9,708	5	11,882
Cost						
Balance at 01/01/06	191	1,537	2,990	16,465	41	21,224
Additions/disposals due to changes in the scope of consolidation		-92	-1	-3,299	-5	-3,397
Additions	62	154			26	242
Transfers		-52			-1	-53
Currency translation adjustments	1	1	61	-108	-4	-49
Disposals	1	89			17	107
Balance at 12/31/06	253	1,459	3,050	13,058	40	17,860
Accumulated amortization/impairment losses						
Balance at 01/01/06	91	838	892	852		2,673
Additions/disposals due to changes in the scope of consolidation		-35		-33		-68
Amortization/impairment losses in the reporting period	30	134	327	6		497
Currency translation adjustments	1		24	-85		-60
Disposals		75				75
Write-backs		8				8
Balance at 12/31/06	122	854	1,243	740		2,959
Carrying amounts						
Balance at 12/31/06	131	605	1,807	12,318	40	14,901

1 Including discontinued operations.

In the reporting period, a total of €74 million (previous year: €73 million) was spent on research and development. Development costs of €52 million (previous year: €62 million) were capitalized. Intangible assets in exploration activities accounted for €209 million in the reporting period (previous year: €101 million).

Goodwill was allocated to cash-generating units at the segment level or at a level beneath the segment level to carry out impairment tests. Goodwill breaks down as follows:

Goodwill € million	12/31/07	12/31/06
RWE Power	829	829
of which: RWE Dea	(30)	(30)
of which: RWE Trading	(434)	(434)
RWE Energy	5,003	5,118
RWE npower	3,876	4,370
Water Division		2,001
	9,708	**12,318**

The goodwill of RWE Energy includes €1,241 million (previous year: €1,270 million) which was recognized in accordance with IAS 32. This goodwill stems from put options granted and forward purchases of minority interests.

In the reporting period, goodwill decreased by €2,090 million (previous year: €3,266 million). Classification of American Water as a discontinued operation resulted in a decline of €1,789 million, and divestments by RWE Energy resulted in disposals of €163 million. In accordance with IAS 12.68, the goodwill of RWE npower was reduced by €138 million (previous year: €48 million), as tax benefits from periods prior to first-time consolidation were realized.

In the period under review, no impairment losses were recognized on goodwill on continued operations (previous year: €6 million). Currency effects decreased the carrying amount of goodwill by €520 million (previous year: €23 million).

The impairment test involves determining the recoverable amount of the cash-generating units, which corresponds to the fair value less costs to sell or the value in use. The fair value reflects the best estimate of the sum that an independent third party would pay to purchase the cash-generating unit as of the balance-sheet date; selling costs are deducted. Value in use is the present value of the future cash flows which are expected to be generated with a cash-generating unit. As of the balance-sheet date, both the fair value less costs to sell and the value in use of the cash-generating units were substantially higher than their carrying amounts.

Fair value and value in use are determined on the basis of a business valuation model, whereby the fair value is assessed from an external perspective and the value in use from a company-internal perspective. Fair values and values in use are determined based on future cash flows, which are based on the business plan for a period of five years, which has been approved by the Executive Board and which is valid when the impairment test is performed. Business plans are based on experience as well as on future expected market trends. If available, market transactions or third-party valuations of similar assets in the same sector are taken as a basis for determining the fair value.

Business plans are based on the general economic data derived from macroeconomic and financial studies and make country-specific assumptions, primarily regarding the development of gross domestic product, consumer prices, interest rates and nominal wages.

The main assumptions underlying the business planning for the divisions active on Europe's electricity and gas markets—RWE Power, RWE Energy and RWE npower—are the premises relating to the development of wholesale prices for electricity, crude oil, natural gas, coal and CO_2 emission allowances, and retail prices for electricity and gas, as well as to the development of market shares and regulatory framework conditions.

The discount rates used for business valuations are determined on the basis of market data and range from 6.5 to 8.5% for cash-generating units after tax (previous year: 5.7 to 6.9%). As in the previous year, the rate generally applied is 6.5%. By contrast, a discount rate of 8.5% is used for RWE Dea, and in the previous year a rate of 5.7% was used in the water business in North America. Before tax, all of the interest rates used are between 9.5 and 13.0% (previous year: 7.5 and 10.5%).

RWE extrapolates future cash flows going beyond the detailed planning horizon based on constant growth rates of 0.0 to 0.5% (previous year: 0.0 to 1.26%), in order to account for expected inflation. These figures are derived from experience and future expectations for each division and do not exceed the long-term average growth rates of the markets on which the companies are active. The cash flow growth rates are determined subtracting the capital expenditure required to achieve the assumed cash flow growth.

(11) Property, plant and equipment[1]

€ million	Land, land rights and buildings incl. buildings on third-party land	Technical plant and machinery	Other equipment, factory and office equipment	Prepayments to other enterprises	Plants under construction	Total
Cost						
Balance at 01/01/07	7,516	64,905	2,157	334	1,562	76,474
Additions/disposals due to changes in the scope of consolidation	-995	-8,040	-132		-211	-9,378
Additions	254	1,806	138	541	1,221	3,960
Transfers	100	732	12	-38	-732	74
Currency translation adjustments	-101	-906	-43		-80	-1,130
Disposals	94	796	177		45	1,112
Balance at 12/31/07	6,680	57,701	1,955	837	1,715	68,888
Accumulated depreciation/impairment losses						
Balance at 01/01/07	3,725	45,073	1,642		0	50,440
Additions/disposals due to changes in the scope of consolidation	-532	-1,789	-74			-2,395
Depreciation/impairment losses in the reporting period	290	1,518	168		59	2,035
Transfers	23	4	-4			23
Currency translation adjustments	-46	-167	-26	1		-238
Disposals	58	775	146		29	1,008
Write-backs	5	2				7
Balance at 12/31/07	3,397	43,862	1,560	1	30	48,850
Carrying amounts						
Balance at 12/31/07	3,283	13,839	395	836	1,685	20,038
Cost						
Balance at 01/01/06	12,158	74,281	2,338	96	1,188	90,061
Additions/disposals due to changes in the scope of consolidation	-5,239	-10,369	-226	14	-47	-15,867
Additions	770	2,522	209	263	752	4,516
Transfers	-4		17	-40	-308	-335
Currency translation adjustments	-58	-576	-10	1	-10	-653
Disposals	111	953	171		13	1,248
Balance at 12/31/06	7,516	64,905	2,157	334	1,562	76,474
Accumulated depreciation/impairment losses						
Balance at 01/01/06	4,899	47,154	1,802		117	53,972
Additions/disposals due to changes in the scope of consolidation	-1,537	-2,849	-180		-120	-4,686
Depreciation/impairment losses in the reporting period	473	1,772	167		1	2,413
Transfers	-7	-112	-1			-120
Currency translation adjustments	-35	-62	3		2	-92
Disposals	60	823	149			1,032
Write-backs	8	7				15
Balance at 12/31/06	3,725	45,073	1,642		0	50,440
Carrying amounts						
Balance at 12/31/06	3,791	19,832	515	334	1,562	26,034

1 Including discontinued operations.

Of additions/disposals due to changes in the scope of consolidation, -€6,865 million (previous year: €0 million) resulted from the disposal of assets held for sale.

Property, plant, and equipment for exploration activities amounted to €212 million in the reporting period (previous year: €118 million).

Property, plant and equipment are subject to restrictions in the amount of €59 million (previous year: €59 million) in the form of land charges and chattel mortgages. Of the carrying amount of property, plant and equipment, €82 million (previous year: €105 million) is attributable to assets leased under finance leases. These assets are principally comprised of technical plant and equipment with a total value of €71 million (previous year: €91 million). Disposal of property, plant and equipment resulted from the sale and decommissioning of plants.

(12) Investment property

€ million	
Cost	
Balance at 01/01/07	438
Additions/disposals due to changes in the scope of consolidation	
Additions	
Transfers	-74
Disposals	31
Balance at 12/31/07	333
Accumulated depreciation/impairment losses	
Balance at 01/01/07	213
Additions/disposals due to changes in the scope of consolidation	
Depreciation/impairment losses in the reporting period	8
Transfers	-23
Disposals	18
Balance at 12/31/07	180
Carrying amounts	
Balance at 12/31/07	153

€ million	
Cost	
Balance at 01/01/06	827
Additions/disposals due to changes in the scope of consolidation	-390
Additions	2
Transfers	19
Disposals	20
Balance at 12/31/06	438
Accumulated depreciation/impairment losses	
Balance at 01/01/06	351
Additions/disposals due to changes in the scope of consolidation	-153
Depreciation/impairment losses in the reporting period	21
Transfers	6
Disposals	12
Balance at 12/31/06	213
Carrying amounts	
Balance at 12/31/06	225

As of December 31, 2007, the fair value of investment property amounted to €264 million (previous year: €331 million). The fair value of investment property is derived from the current market prices of comparable real estate or determined using internationally accepted valuation methods such as the discounted cash flow method. €79 million of the fair value (previous year: €90 million) is based on valuations made by independent appraisers. Rental income in the reporting period amounted to €15 million (previous year: €48 million). Direct operating expenses totalled €8 million (previous year: €23 million).

(13) Investments accounted for using the equity method

The following summaries present the key items from the balance sheets and income statements of companies accounted for using the equity method:

Investments accounted for using the equity method € million	12/31/07	12/31/06
Equity		
Assets	16,287	17,447
Liabilities	10,718	11,295
	5,569	**6,152**
Adjustment to RWE interest and equity method	-3,148	-3,881
	2,421	**2,271**

Income from investments accounted for using the equity method € million	2007	2006
Revenue	13,042	10,908
Income	980	703
Adjustment to RWE interest and equity method	-533	-294
	447	**409**

As of December 31, 2007 the fair value of investments accounted for using the equity method for which quoted market prices exist amounted to €3 million (previous year: €3 million).

(14) Other non-current financial assets

€ million	12/31/07	12/31/06
Non-consolidated subsidiaries	220	173
Other investments	347	464
Non-current securities	444	1,047
	1,011	**1,684**

Non-current securities primarily consist of fixed-interest marketable securities and shares of public companies. They are not subject to any restrictions on disposal. The fair value of the other financial assets essentially corresponds to their carrying amounts.

(15) Financial receivables

€ million	12/31/07		12/31/06	
	Non-current	Current	Non-current	Current
Loans to non-consolidated subsidiaries and investments	833	82	970	39
Collaterals for trading activities		1,118		2,426
Other financial receivables				
Deferred interest		130		117
Miscellaneous other financial receivables	505	372	567	363
	1,338	**1,702**	**1,537**	**2,945**

As of the balance-sheet date, financial receivables from associates amounted to €856 million (previous year: €1,089 million).

RWE Group companies must deposit the collaterals for the trading activities stated above, pursuant to the regulations of the EEX and for over-the-counter (OTC) transactions. These guarantees are designed to ensure that the obligations from the transactions are discharged even if the development of prices is not favourable.

(16) Other receivables and other assets

€ million	12/31/07		12/31/06	
	Non-current	Current	Non-current	Current
Derivatives	646	6,038	445	6,040
Surplus of plan assets over benefit obligations	773		419	
Prepayments for items other than inventories		283		250
CO_2 emission allowances		390		408
Prepaid expenses		116		136
Miscellaneous other assets	274	707	229	839
	1,693	**7,534**	**1,093**	**7,673**

With the exception of derivatives, the financial instruments reported under other receivables and other assets are measured at amortized cost. This essentially corresponds to their fair value. Derivative financial instruments are stated at fair value.

The carrying values of exchange-traded derivatives with netting agreements are offset in accordance with IAS 32.42.

Changes in the scope of consolidation reduced other receivables and other assets by €47 million.

(17) Income tax assets

On December 13, 2006, upon entry into force of the act on fiscal measures accompanying the introduction of the European Company and the amendment of other fiscal regulations (SEStEG), a legally unconditional claim was created as of December 31, 2006 for the refund of corporate tax credits stemming from the previous tax credit system (cf. Sec. 37 of the German Corporate Income Tax Act, as amended, KStG). This resulted in tax income of €636 million in the previous year. The distribution-dependent realization of the credit applicable in the past was replaced by a procedure by which payments are made in instalments over a period of 10 years (2008 to 2017; generally effective September 30). Since the instalments do not bear interest, the receivable is stated at its present value.

(18) Deferred taxes

The deferred tax assets of €2,456 million (previous year: €3,618 million) and deferred tax liabilities of €1,928 million (previous year: €3,077 million) principally relate to measurements deviating from the tax bases. €1,734 million and €1,346 million of the total amount of gross deferred tax assets and liabilities, respectively, will be realized within twelve months (previous year: €2,488 million and €1,997 million).

The following is a breakdown of deferred tax assets and liabilities by item:

Deferred taxes € million	12/31/07		12/31/06	
	Assets	Liabilities	Assets	Liabilities
Non-current assets	347	2,140	197	3,482
Current assets	140	497	155	1,081
Exceptional tax items		309		453
Non-current liabilities				
Provisions for pensions	204	71	971	11
Other non-current provisions	1,648	76	2,010	117
Current liabilities	1,594	849	2,333	916
	3,933	**3,942**	**5,666**	**6,060**
Tax loss carryforwards	537		935	
Gross total	**4,470**	**3,942**	**6,601**	**6,060**
Netting	-2,014	-2,014	-2,983	-2,983
Net total	**2,456**	**1,928**	**3,618**	**3,077**

Deferred tax assets and deferred tax liabilities are netted out for each company and/or tax group.

Total deferred tax assets include the following capitalized tax reduction claims which result from the expected utilization of previously unused tax loss carryforwards in subsequent years:

Tax reduction claims from loss carryforwards € million	12/31/07	12/31/06
Corporate income tax (or comparable foreign income tax)	186	509
Trade tax	351	426
	537	**935**

The realization of these tax carryforwards is guaranteed with sufficient certainty. At the end of the reporting period, there were €467 million in corporate income tax loss carryforwards and €494 million in trade tax loss carryforwards for which no deferred tax claims have been recognized (previous year: €489 million and €735 million, respectively).

Domestic and foreign tax loss carryforwards can be used for an unlimited period.

In the year under review, €132 million in deferred taxes (previous year: €50 million) arising from the translation of foreign financial statements and -€141 million (previous year: €66 million) from valuations without an effect on income were offset against equity.

(19) Inventories

€ million	12/31/07	12/31/06
Raw materials, incl. nuclear fuel assemblies and earth excavated for lignite mining	1,478	1,283
Work in progress-goods	20	31
Work in progress-services	68	51
Finished goods and goods for resale	771	849
Prepayments	15	12
	2,352	**2,226**

Inventories were not subject to any restrictions on disposal and there were no further obligations.

Changes in the scope of consolidation resulted in a decrease of €35 million in inventories.

(20) Trade accounts receivable

As of the balance-sheet date, trade accounts receivable from associates amounted to €300 million (previous year: €389 million).

A decrease of €272 million in trade accounts receivable is attributable to changes in the scope of consolidation.

(21) Marketable securities

The total value of current marketable securities was €10,858 million (previous year: €16,788 million), consisting of fixed-interest marketable securities of €9,685 million (previous year: €14,075 million) with a maturity of more than three months from the date of acquisition, and stocks and profit-participation certificates of €1,173 million (previous year: €2,713 million). Marketable securities are stated at fair value. As of December 31, 2007, the average return obtainable on fixed-interest securities was 4.9% (previous year: 4.1%).

(22) Cash and cash equivalents

€ million	12/31/07	12/31/06
Cash	1,386	2,570
Marketable securities and other cash investments (maturity less than three months from the date of acquisition)	536	224
	1,922	**2,794**

Demand deposits are only kept for short-term cash positions at banks with a minimum rating of A-/A3. As in the previous year, interest rates are maintained at interbank levels.

(23) Equity

A breakdown of equity is shown on page 142.

Subscribed capital is structured as follows:

Subscribed capital	12/31/07 Number of shares '000	%	12/31/06 Number of shares '000	%	12/31/07 € million	12/31/06 € million
Common shares	523,405	93.1	523,405	93.1	1,340	1,340
Preferred shares	39,000	6.9	39,000	6.9	100	100
	562,405	**100.0**	**562,405**	**100.0**	**1,440**	**1,440**

Common and preferred shares are no-par value bearer share certificates. Preferred shares have no voting rights. Under certain conditions, preferred shares are entitled to payment of a preference dividend of €0.13 per preferred share, upon allocation of the Company's profits.

The contingent capital of €51,200,000 available as of December 31, 2006 to offer subscription rights to common shares in the name of the bearer to members of the Executive Board as well as to other executives of RWE AG and subordinate affiliates has ceased to exist. RWE AG's Articles of Incorporation were reworded accordingly, pursuant to a Supervisory Board resolution.

Pursuant to the resolution passed by the Annual General Meeting on April 18, 2007, the Executive Board was authorized to purchase shares of any class in RWE, totalling up to 10% of the company's share capital until October 17, 2008. In addition, authorization was granted to acquire the company's shares by exercising put or call options.

Accumulated other comprehensive income reflects changes in the fair values of financial instruments available for sale and of cash flow hedges as well as such stemming from foreign currency translation adjustments from foreign financial statements.

In the year under review, €16 million in changes in the fair values of instruments used for cash flow hedges (previous year: -€784 million) were disclosed under accumulated other comprehensive income without an effect on income. These changes in value reflect the effective portion of the hedges. In fiscal 2007, €4 million in changes in the value of financial instruments available for sale (previous year: €139 million) were also recognized under accumulated other comprehensive income without an effect on income. €225 million in cash flow hedges were realized as expenses (previous year: income of €7 million) and €336 million in "financial instruments available for sale" were realized as income (previous year: €247 million).

Dividend proposal

We propose to the Annual General Meeting that RWE AG's distributable profit for fiscal 2007 be appropriated as follows:

Distribution of a dividend of €3.15 per individual, dividend-bearing share:

Dividend	€1,771,575,750.00
Profit carryforward	€10,872.55
Distributable profit	€1,771,586,622.55

Minority interest

The share ownership of third parties in Group entities is presented in this item. In particular, there are significant minority interests in the Hungarian energy utilities and in the Czech gas companies.

(24) Share-based payment

In the year under review, the groupwide share-based payment systems for executives of RWE AG and subordinate affiliates consisted of the following: the Long-Term Incentive Plan (LTIP) and Beat. If the persons holding stock options are not employed by RWE AG, the expenses associated with the exercise of the options are borne by the respective Group company.

	LTIP[1]		
	2002 tranche	2003 tranche	2004 tranche
Grant date	09/20/2002	07/01/2003	05/25/2004
Number of options granted	5,950,350	6,677,450	9,192,800
Term	5 years	5 years	5 years
Vesting conditions	Two-year waiting period; the common share price must have risen by at least 10% prior to the exercise date and must have outperformed the Dow Jones STOXX Utilities Price Index on ten consecutive days in the same period (this last condition does not apply if the common share price increases by at least 20%). Upon achievement of the above performance targets, the options can be exercised on a daily basis following expiration of the waiting period, with the exception of short blocking periods prior to the publication of corporate data. The number of options which may be exercised depends on the increase in the price of the common share compared to the exercise price determined when the options are granted. In the event of a 20% price increase all of the options can be exercised; for a 15 or 10% increase, 60 or 25% of the options can be exercised, respectively.		
Exercise price	€34.24	€26.37	€35.45
Form of settlement	Cash settlement amounting to the difference between the share price upon exercise and the exercise price or provision of common shares (at the discretion of RWE AG). Settlement is limited to 50% of the exercise price.		

1 Long-Term Incentive Plan.

	Beat		
	2005 tranche	2006 tranche	2007 tranche
Grant date	01/01/2005	01/01/2006	01/01/2007
Number of conditionally granted performance shares	2,551,800	2,444,191	1,468,132
Term	3 years	3 years	3 years
Pay-out conditions	Automatic pay-out if following a waiting period of three years an outperformance of at least 25% compared to the Dow Jones STOXX Utilities Index peer group has been achieved, measured in terms of their index weighting as of the inception of the programme. Measurement of outperformance is carried out using Total Shareholder Return (TSR), which takes into account both the development of the share price and reinvested dividends.		
Determination of payment	1. Determination of the index weighting of the peer group companies which exhibit a lower TSR than RWE at the end of the term. 2. Performance factor is calculated by squaring this percentage rate and multiplying it by 1.25. 3. Total number of performance shares which can be paid out is calculated by multiplying the performance shares conditionally granted by the performance factor. 4. Payment corresponds to the final number of performance shares valued at the average RWE share price during the last 20 trading days prior to expiration of the programme (with a ceiling of two times and three times the value of the performance shares as of the grant date, for the 2006 and 2007 tranche, and the 2005 tranche, respectively).		
Change in corporate control/merger	▪ If during the waiting period there is a change in corporate control, a compensation payment is made. This is calculated by multiplying the price paid in the acquisition of the RWE shares by the final number of performance shares. The latter shall be determined as per the regulations of the compensation plan with regard to the time when the bid for corporate control is submitted. ▪ In the event of merger with another company, compensation shall be calculated on the basis of the expected value of the performance shares at the time of the merger multiplied by the prorated number of performance shares corresponding to the ratio between the total waiting period and the waiting period until the merger takes place.		
Form of settlement	Cash settlement		

Long-Term Incentive Plan. The following changes in the number of outstanding LTIP options occurred in the year under review:

LTIP	2002 tranche	2003 tranche	2004 tranche
Outstanding at the start of the fiscal year	1,200	24,200	116,850
Change in grant / expired	-1,200	-3,000	5,000
Exercised	0	-8,000	-36,850
Outstanding at the end of the fiscal year	0	13,200	85,000
Exercisable at the end of the fiscal year	0	13,200	85,000

The average weighted share price as of the exercise date amounted to €80.63 for the options from LTIP exercised in fiscal 2007. The exercise prices of the outstanding LTIP options as of the balance-sheet date ranged between €13.19 and €17.73. The weighted average remaining contractual term amounted to 1.4 years.

Beat. The fair value of the performance shares conditionally granted in the Beat programme amounted to €24.99 per share as of the grant date for the 2007 tranche, €17.48 per share for the 2006 tranche and €18.62 per share for the 2005 tranche. These values were calculated externally using a standard multivariate Black-Scholes model via Monte Carlo simulations on the basis of one million scenarios each. In the calculations, due consideration was taken of the maximum payment stipulated in the programme's conditions for each conditionally granted performance share, the discount rates for the remaining term, the volatilities and the expected dividends of peer companies as well as the expected dividends of RWE AG.

In the year under review, the number of performance shares issued in the Beat programme developed as follows:

Beat	2005 tranche	2006 tranche	2007 tranche
Outstanding at the start of the fiscal year	2,287,886	2,429,155	0
Granted			1,468,132
Change in grant / expired	-4,768	-7,794	-4,582
Outstanding at the end of the fiscal year	2,283,118	2,421,361	1,463,550
Payable at the end of the fiscal year	2,283,118	0	0

The remaining contractual term amounted to one year for the 2006 tranche and two years for the 2007 tranche. The contractual term for the 2005 tranche ended upon completion of the year under review. In accordance with the plan regulations, the payment amount is determined based on a share price of €55.86.

In addition to the above, the following share-based payment systems with equity settlement for executives and employees are operated at the level of the divisions:

RWE Npower plc/RWE Trading GmbH/ RWE Systems UK Ltd.	LTIP	Sharesave Scheme
Awards/tranches	2005	2003 - 2007
Number of options granted per tranche	130,608	228,335 - 787,875
Term	3 years	3 years
Vesting conditions	Waiting period: 2 years	Waiting period: 3 years
Exercise price	€1.46	€19.90 - 59.37
Form of settlement	Existing shares	Existing shares

In the year under review, the number of outstanding LTIP options developed as follows:

RWE Npower plc/ RWE Trading GmbH	LTIP
Outstanding at the start of the fiscal year	88,778
Exercised	-88,778
Outstanding at the end of the fiscal year	0
Exercisable at the end of the fiscal year	0

In the year under review, the number of outstanding Sharesave Scheme options developed as follows:

RWE Npower plc/RWE Trading GmbH/ RWE Systems UK Ltd.	Sharesave Scheme
Outstanding at the start of the fiscal year	934,960
Granted	247,119
Exercised	-188,087
Expired	-51,735
Outstanding at the end of the fiscal year	942,257
Exercisable at the end of the fiscal year	12,412

The total expense for the groupwide share-based payment systems amounted to €72 million (previous year: €94 million) in fiscal 2007. Of this amount, €0 million was attributable to equity-settled share-based payment transactions of RWE AG, as in the previous year. As of the balance-sheet date, provisions in the amount of €168 million have been recognized for cash-settled share-based payment programmes (previous year: €97 million). The intrinsic value of the cash-settled share-based payment transactions exercisable or payable as of the balance-sheet date amounted to €129 million (previous year: €2 million).

(25) Provisions[1]

€ million	12/31/07			12/31/06		
	Non-current	Current	Total	Non-current	Current	Total
Provisions for pensions and similar obligations	3,496		3,496	11,584		11,584
Provisions for taxes	2,548	687	3,235	2,095	630	2,725
Provisions for nuclear waste management	8,847	206	9,053	8,544	290	8,834
Provisions for mining damage	2,741	81	2,822	2,468	80	2,548
	17,632	**974**	**18,606**	**24,691**	**1,000**	**25,691**
Other provisions						
Staff-related obligations (excluding restructuring)	703	797	1,500	829	925	1,754
Restructuring obligations	478	169	647	553	252	805
Purchase and sales obligations	635	1,159	1,794	674	1,004	1,678
Uncertain obligations in the electricity business	467	463	930	423	343	766
Environmental protection obligations	122	31	153	126	25	151
Interest payment obligations	435	173	608	398	53	451
CO_2 emission allowances		390	390		253	253
Miscellaneous other provisions	740	1,557	2,297	938	1,579	2,517
	3,580	**4,739**	**8,319**	**3,941**	**4,434**	**8,375**
	21,212	**5,713**	**26,925**	**28,632**	**5,434**	**34,066**

1 Including discontinued operations.

Provisions for pensions and similar obligations. The company pension plan consists of defined contribution and defined benefit plans. In the reporting period, payments to defined contribution plans amounted to €11 million (previous year: €12 million).

At the end of March 2007, €7,856 million in assets were transferred to the trust RWE Pensionstreuhand e.V. to externally finance parts of the corporate pension plan via a contractual trust arrangement (CTA). Since the transferred assets are classified as plan assets as defined by IAS 19, provisions for pensions and similar obligations were netted out against the transferred assets as of March 31, 2007. As a result, provisions for pensions and similar obligations declined by €7,768 million, and the surplus of plan assets over benefit obligations stated under “Other assets” increased by €88 million. The transferred assets consist of the balance-sheet items “Other financial assets” (€3,702 million) and “Marketable securities”

(€4,154 million). Since this was a non-cash transaction, it did not have an impact on the cash flow statement.

As of November 1, 2007, RWE AG transferred certain benefit obligations to RWE Pensionsfonds AG. In the future, this non-insurance-based pension fund will be responsible for the corporate pension plan benefits for this group of beneficiaries.

The amount of provisions for defined benefit plans was calculated using actuarial methods, using the so-called corridor approach. The following assumptions are applied:

Calculation assumptions %	12/31/07		12/31/06	
	Germany	Foreign[2]	Germany	Foreign
Discount rate	5.50	5.95	4.50	5.10 - 5.90
Compensation increase	2.75	4.80	2.75	4.00 - 5.00
Pension increase	1.00 - 1.50	3.30	1.00 - 1.50	3.10
Rise in health care cost trend[1]				5.00 - 9.00
Expected return on the plan assets	5.75	7.00		6.10 - 8.75

1 Not relevant for recognized plans as of December 31, 2007.
2 Pertains to RWE npower.

The expected return on plan assets was determined depending on the specific asset categories. The expected return on investments in equities reflects the long-term average performance observed for the industries and geographical markets involved, taking into account the current composition of the equity portfolio. The expected return on fixed-interest securities was derived from appropriately selected trading prices and indices, in accordance with recognized methods. The expected return on real estate was calculated on the basis of marketing possibilities determined by contractual obligations and local market conditions.

Provisions for pensions are broken down as follows:

Provisions for pensions and similar obligations (funded and unfunded plans) € million	12/31/07		12/31/06	
Present value of funded benefit obligations	**12,298**		**6,569**	
Fair value of plan assets	12,675		6,119	
Unrecognized net actuarial gains (losses)	-351		-532	
Net amount recognized for funded benefit plans		-728		-82
Capitalized surplus of plan assets over benefit obligations		773		419
Provision recognized for funded plans		**45**		**337**
Present value of unfunded benefit obligations	**3,428**		**11,386**	
Unrecognized net actuarial gains (losses) on unfunded plans	23		-139	
Provision recognized for unfunded plans		**3,451**		**11,247**
		3,496		**11,584**

The unrecognized actuarial gains (losses) of -€328 million (previous year: -€671 million) primarily result from actuarial gains (losses) in connection with unexpected fluctuations and differences in actual market trends compared with the actuarial assumptions. In accordance with the corridor method which is currently still being applied, this amount is recognized as income or an expense over the anticipated average remaining working lives of the employees, to the extent that it exceeds 10% of the greater of the benefit obligation or the fair value of the plan assets. Starting from fiscal 2008, actuarial gains and losses will be recognized directly in consolidated equity outside profit or loss, in accordance with IAS 19.93A.

Development of plan assets € million	Fair value 2007	Fair value 2006
Balance at 01/01	6,119	7,692
Expected return on plan assets	684	400
Employer contributions to the funded plans	8,129	179
Employee contributions to the funded plans	13	31
Benefits paid by the funded plans	-667	-402
Actuarial gains (losses) related to plan assets	-494	-69
Currency translation adjustments	-529	67
Changes in the scope of consolidation	-580	-1,779
Balance at 12/31	**12,675**	**6,119**

The actual return on plan assets amounted to €190 million (previous year: €331 million).

Composition of plan assets (fair value) € million	12/31/07 Germany[1]	 Foreign[2]	 Total	12/31/06 Germany	 Foreign	 Total
Equity capital instruments	1,870	526	2,396		1,635	1,635
Interest-bearing instruments	4,979	3,249	8,228		3,633	3,633
Real estate		313	313		377	377
Alternative investments	631	859	1,490		272	272
Other[3]	248		248	81	121	202
	7,728	**4,947**	**12,675**	**81**	**6,038**	**6,119**

1 Plan assets in Germany primarily pertain to assets of RWE AG and assets of RWE Pensionsfonds AG which are managed by RWE Pensionstreuhand e.V. as a trust.
2 Foreign plan assets pertain to the assets of a UK pension fund for covering benefit commitments to employees of the RWE Group in the UK.
3 Includes reinsurance claims vis-à-vis insurance companies.

Composition of plan assets (targeted investment structure) %	12/31/07 Germany[1]	 Foreign[2]	12/31/06 Foreign
Equity capital instruments	29.0	10.6	27.1
Interest-bearing instruments	58.0	65.7	60.2
Real estate	3.0	6.3	6.2
Alternative investments	10.0	17.4	4.5
Other[3]			2.0
	100.0	**100.0**	**100.0**

1 Plan assets in Germany primarily pertain to assets of RWE AG and assets of RWE Pensionsfonds AG which are managed by RWE Pensionstreuhand e.V. as a trust.
2 Foreign plan assets pertain to the assets of a UK pension fund for covering benefit commitments to employees of the RWE Group in the UK.
3 Does not include reinsurance claims vis-à-vis insurance companies, as such do not fall under the scope of portfolio management as a whole.

Development of pension claims € million	Present value 2007	 2006
Balance at 01/01	17,955	20,642
Current service cost	213	241
Interest cost	837	895
Contributions by employees	28	31
Actuarial gains (losses)	-752	-545
Benefits paid	-986	-961
Past service cost	-161	-199
Currency translation adjustments	-574	25
Changes in the scope of consolidation	-834	-2,174
Balance at 12/31	**15,726**	**17,955**

The past service costs recognized for the reporting period stem principally from the increase in the statutory retirement age, due to amendment of the German law on the minimum pensionable age. This amendment results in a reduction of the period of pension benefit payments taken as a basis for the pension provisions, as employees in the RWE Group must generally draw a statutory pension to be eligible for a company pension.

Expenses for pension provisions[1] € million	2007	2006
Service cost	178	160
Interest cost	784	761
Expected return on plan assets	-635	-257
Amortization of past service cost	-161	-199
Recognized net actuarial gains (losses)	13	17
	179	**482**

1 Excluding discontinued operations.

Since 2005, the present value of pension claims, the fair value of plan assets and the surplus or deficit of the plan have developed as follows:

€ million	2007	2006	2005
Present value of pension claims	**15,726**	**17,955**	**20,642**
Fair value of plan assets	**12,675**	**6,119**	**7,692**
Unrecognized net actuarial gains (losses)	-328	-671	-1,507
Plan surplus/deficit	**2,723**	**11,165**	**11,443**
of which: surplus of plan assets over benefit obligations	(773)	(419)	(554)
of which: provisions for pensions	(3,496)	(11,584)	(11,997)

For the reporting period and the previous years, the following experience adjustments were made to the present value of the pension claims and the fair value of the plan assets:

Experience adjustments € million	2007	2006	2005
Present value of pension claims	367	38	-61
Fair value of plan assets	-494	-69	550

Experience adjustments to the present value of pension claims represent part of the actuarial gains or losses arising on the pension claims for the year in question. Experience adjustments to the fair value of plan assets are to be equated with the actuarial gains or losses arising on the plan assets for the year in question.

Payments for defined benefit plans are expected to amount to €157 million in fiscal 2008.

Roll-forward of provisions € million	Balance at 01/01/07	Additions	Unused amounts released	Interest accretion/ change in discount rate	Changes in the scope of conso-lidation, currency adjust-ments, transfers	Amounts used	Balance at 12/31/07
Provisions for pensions	11,584	53	-2	265	-8,005	-399	3,496
Provisions for taxes	2,725	1,104	-41		-3	-550	3,235
Provisions for nuclear waste management	8,834	128	-178	425		-156	9,053
Provisions for mining damage	2,548	210	-5	123	-2	-52	2,822
	25,691	**1,495**	**-226**	**813**	**-8,010**	**-1,157**	**18,606**
Other provisions							
Staff-related obligations (excluding restructuring)	1,754	619	-135	13	-59	-692	1,500
Restructuring obligations	805	43	-27	10	-4	-180	647
Purchase and sales obligations	1,678	956	-298	19	1	-562	1,794
Uncertain obligations in the electricity business	766	141	-29	-3	161	-106	930
Environmental protection obligations	151	12	-1	1	-6	-4	153
Interest payment obligations	451	139	-9		54	-27	608
CO_2 emission allowances	253	265			-16	-112	390
Miscellaneous other provisions	2,517	827	-192	34	-482	-407	2,297
	8,375	**3,002**	**-691**	**74**	**-351**	**-2,090**	**8,319**
Provisions	**34,066**	**4,497**	**-917**	**887**	**-8,361**	**-3,247**	**26,925**
of which: changes in the scope of consolidation							(-319)

The vast majority of ***provisions for nuclear waste management*** are recognized as non-current provisions, and their settlement amount is discounted to the balance-sheet date. As in the previous year, an interest rate of 5.0% was used as the discount rate. Volume-based increases in the provisions are measured at their present value. In the reporting period, they amounted to €128 million (previous year: €92 million). By releasing €178 million in unused provisions (previous year: €164 million), we have taken into account that waste disposal costs are expected to be lower, according to current estimates. Additions to provisions for nuclear waste management primarily consist of an interest accretion of €425 million (previous year: €416 million). €684 million in prepayments, primarily to foreign reprocessing companies and to the German Federal Office for Radiation Protection (BfS) for the construction of final storage facilities, were deducted from the provisions for nuclear waste management (previous year: €640 million).

In terms of their contractual definition, provisions for nuclear waste management break down as follows:

Provisions for nuclear waste management € million	12/31/07	12/31/06
Provisions for nuclear obligations, not yet contractually defined	7,159	6,895
Provisions for nuclear obligations, contractually defined	1,894	1,939
	9,053	**8,834**

In respect of the disposal of spent nuclear fuel assemblies, the provisions for obligations which are not yet contractually defined cover the estimated long-term costs of direct final storage of fuel assemblies, which is currently the only possible disposal method in Germany, and the costs for the disposal of radioactive waste from reprocessing. The latter essentially consist of costs for transport from centralized storage facilities and the plants' intermediate storage facilities to reprocessing plants and final storage as well as conditioning for final storage and containers. These estimates are mainly based on studies by internal and external experts, in particular by Gesellschaft für Nuklear-Service mbH (GNS) in Essen, Germany. With regard to the decommissioning of nuclear power plants, the costs for the post-operational phase and dismantling are taken into consideration, on the basis of data from external expert opinions prepared by NIS Ingenieurgesellschaft mbH, Alzenau, Germany, which are generally accepted throughout the industry and are updated continuously. Finally, this item also covers all of the costs of final storage for all radioactive waste, based on data provided by BfS.

Provisions for contractually defined nuclear obligations are related to all nuclear obligations for the disposal of fuel assemblies and radioactive waste as well as for decommissioning, insofar as the value of said obligations is specified in contracts under civil law. They include the anticipated residual costs of reprocessing, return (transport, containers) and intermediate storage of the resulting radioactive waste, as well as the additional costs of the utilization of uranium and plutonium from reprocessing activities. These costs are based on existing contracts with foreign reprocessing companies and with GNS. Moreover, these provisions also take into account the costs for transport and intermediate storage of spent fuel assemblies within the framework of final direct storage. The power plants' intermediate storage facilities are licensed for an operational period of 40 years and commenced operations between 2002 and 2006. Furthermore, the amounts are also stated for the conditioning and intermediate storage of radioactive operational waste, which is primarily performed by GNS.

With due consideration of the German Atomic Energy Act (AtG), in particular to Sec. 9a of AtG, the provision for nuclear waste management breaks down as follows:

Provisions for nuclear waste management € million	12/31/07	12/31/06
Decommissioning of nuclear facilities	4,443	4,213
Disposal of nuclear fuel assemblies	4,061	4,168
Disposal of radioactive operational waste	549	453
	9,053	**8,834**

Provisions for mining damage also consist primarily of non-current provisions. They are recognized at the settlement amount discounted to the balance-sheet date. As in the previous year, an interest rate of 5.0% was used as the discount rate. In the reporting period, additions to provisions for mining damage amounted to €210 million (previous year: €151 million). Of this, an increase of €128 million (previous year: €108 million) did not have an impact on income, as an identical amount was capitalized under property, plant and equipment. The interest accretion of the additions to provisions for mining damage amounted to €123 million (previous year: €113 million).

Provisions for restructuring pertain mainly to measures for socially acceptable payroll downsizing from previous years.

(26) Financial liabilities

€ million	12/31/07		12/31/06	
	Non-current	Current	Non-current	Current
Bonds payable (incl. other notes payable)	9,029	1,622	14,507	1,873
Commercial paper				546
Bank debt	564	790	754	628
Other financial liabilities				
Collaterals for trading activities		404		172
Miscellaneous other liabilities	453	423	411	491
	10,046	**3,239**	**15,672**	**3,710**

Financial liabilities to associates totalled €97 million (previous year: €105 million).

€9,886 million of the non-current financial liabilities were interest-bearing liabilities (previous year: €15,233 million). To a great degree, bank debt stems from the former activities of acquired companies. Nominal interest depends on the currency, term and conditions of the agreement and ranges between 2.0 and 9.0% as in the previous year.

Changes in the scope of consolidation caused financial liabilities to decrease by €3,513 million.

Outstanding bonds payable relate to RWE AG and RWE Finance B.V. Nominal interest is between 2.0 and 6.5% for public bonds (previous year: 0 and 8.0%), and between 2.3 and 7.0% (previous year: 0.78 and 10.0%) for private placements (depending on currency, term and time of issue).

The following table presents the structure of our major bonds payable as of December 31, 2007:

Issuer	Outstanding amount	Carrying amount	Coupon in %	Maturity
RWE AG	€ 86 million	€ 86 million	5.625	June 2009
RWE AG	€ 100 million	€ 100 million	variable[1]	November 2017
RWE AG	€ 600 million	€ 593 million	5.75	February 2033
RWE Finance B.V.	€ 1,282 million	€ 1,281 million	5.375	April 2008
RWE Finance B.V.	CHF 500 million	€ 302 million	2.0	December 2008
RWE Finance B.V.	£ 500 million	€ 682 million	4.625	August 2010
RWE Finance B.V.	€ 1,808 million	€ 1,845 million	6.125	October 2012
RWE Finance B.V.	£ 630 million	€ 856 million	6.375	June 2013
RWE Finance B.V.	€ 530 million	€ 527 million	4.625	July 2014
RWE Finance B.V.	€ 850 million	€ 853 million	6.25	April 2016
RWE Finance B.V.	€ 980 million	€ 975 million	5.125	July 2018
RWE Finance B.V.	£ 570 million	€ 781 million	6.5	April 2021
RWE Finance B.V.	£ 488 million	€ 662 million	5.625	December 2023
RWE Finance B.V.	£ 760 million	€ 1,035 million	6.25	June 2030
Other (incl. other notes payable)	Various	€ 73 million	Various	Various
Bonds payable (incl. other notes payable)		**€ 10,651 million**		

1 Interest payment dates: May 15 /Nov. 15.

As of the balance-sheet date, € 10,429 million (previous year: € 15,606 million) of the financial liabilities were allocated to the category liabilities stated at (amortized) cost. The fair value amounted to € 10,712 million (previous year: € 16,494 million).

During the reporting period, commercial paper was occasionally issued on the European and US capital markets. Up to € 0.5 billion was raised within the framework of this programme (previous year: € 4.0 billion). The interest rates ranged between 3.59 and 4.26% (previous year: 2.34 and 5.62%). RWE AG had no commercial paper outstanding as of the cut-off date (previous year: € 546 million).

Other financial liabilities primarily consist of finance lease liabilities. Lease agreements principally relate to capital goods in the electricity and water business.

Liabilities arising from finance lease agreements have the following maturities:

Liabilities from finance lease agreements	Maturities of minimum lease payments					
	12/31/07			12/31/06		
€ million	Nominal value	Discount	Present value	Nominal value	Discount	Present value
Due within one year	17	2	15	16	1	15
Due within one to five years	57	2	55	66	11	55
Due after five years	99	50	49	37	11	26
	173	**54**	**119**	**119**	**23**	**96**

Above and beyond this, other financial liabilities include collaterals for trading activities which must be deposited with RWE Group companies by our business partners pursuant to the regulations of the European Energy Exchange in Leipzig, and for OTC transactions.

€ 84 million (previous year: € 125 million) of the financial liabilities are secured by mortgages, and € 11 million (previous year: € 13 million) by similar rights.

(27) Trade accounts payable

Accounts payable to associates amounted to € 71 million (previous year: € 90 million).

Trade accounts payable generally have short remaining maturities. Accordingly, the amounts recognized approximately correspond to the fair value of these liabilities.

Exploration activities resulted in liabilities of € 81 million (previous year: € 57 million).

Changes in the scope of consolidation resulted in a € 1,063 million decrease in trade accounts payable.

(28) Other liabilities

	12/31/07		12/31/06	
€ million	Non-current	Current	Non-current	Current
Tax liabilities		514		446
Social security liabilities	305	170	361	171
Derivatives	304	5,774	643	6,334
Deferred income	2,088	362	3,175	310
Miscellaneous other liabilities	887	2,149	842	2,266
	3,584	**8,969**	**5,021**	**9,527**

The principle component of social security liabilities are the amounts payable to social security institutions.

Deferred income	12/31/07		12/31/06	
€ million	Non-current	Current	Non-current	Current
Advances and contributions in aid of construction and building connection	1,894	171	2,992	163
Government grants for non-current assets				
Taxable	14	2	15	2
Non-taxable	1			
Other	179	189	168	145
	2,088	**362**	**3,175**	**310**

Miscellaneous other liabilities include €792 million (previous year: €777 million) in non-current redemption liabilities and, as in the previous year, €1,159 million in current redemption liabilities from put options and forward purchases of minority interests that are recognized in accordance with IAS 32.

The financial instruments reported under miscellaneous other liabilities generally have short remaining maturities. Accordingly, the amounts recognized approximately correspond to the fair values. Derivative financial instruments are stated at fair value.

Other information

(29) Earnings per share

Basic and diluted earnings per share are calculated by dividing the net income attributable to the shares by the average number of shares outstanding. The earnings per share are the same for both common and preferred shares.

Earnings per share		2007	2006
Net income	€ million	2,659	3,847
Number of shares outstanding (weighted average)	thousands	562,373	562,374
Basic and diluted earnings per common and preferred share	€	4.73	6.84
Dividend per share	€	3.15[1]	3.50

1 Proposal for fiscal 2007.

(30) Reporting on financial instruments

Financial instruments are divided into non-derivative and derivative financial instruments.

Non-derivative financial assets essentially include other non-current financial assets, accounts receivable, marketable securities and cash and cash equivalents. Financial assets available for sale are measured at fair value, while other financial assets are measured at amortized cost. On the liabilities side, non-derivative financial instruments principally include liabilities recorded at amortized cost. The balance of non-derivative financial instruments is disclosed in the balance sheet, and the maximum default risk corresponds to the amount of financial assets. If default risks associated with financial assets are identified, they are recognized through impairment.

Fair values are derived from the relevant stock market quotations or are measured using generally accepted valuation methods. Trading prices on active markets (e.g. exchange prices) are drawn upon for the measurement of commodity derivatives. If no trading prices are available, for example because the market is not sufficiently liquid, the fair values are determined on the basis of generally accepted valuation methods. In doing so, trading prices on active markets are drawn upon as input parameters as much as possible. If such trading prices are not available, company-specific planning estimates are used in the measurement process. These estimates contain all of the market factors which other market participants would take into account in the course of price determination.

Impairments on receivables reported under the following balance-sheet items developed as follows:

Impairments on receivables 2007 € million	Other non-current financial assets	Financial receivables	Trade accounts receivable	Other receivables and other assets	Total
Balance at 01/01/07	214	72	433	3	722
Additions/disposals due to changes in the scope of consolidation	2	-2			0
Impairments in the reporting period	3	138	139	1	281
Transfers	-60	60			0
Currency translation adjustments	1		-27		-26
Disposals	46	3	97	1	147
Balance at 12/31/07	**114**	**265**	**448**	**3**	**830**

Impairments on receivables 2006 € million	Other non-current financial assets	Financial receivables	Trade accounts receivable	Other receivables and other assets	Total
Balance at 01/01/06	178	74	271		523
Additions/disposals due to changes in the scope of consolidation	-1	-11			-12
Impairments in the reporting period	47	1	196	2	246
Transfers	3	9	5	1	18
Currency translation adjustments			8		8
Disposals	13	1	47		61
Balance at 12/31/06	**214**	**72**	**433**	**3**	**722**

As of the cut-off date, unimpaired, past due receivables were recorded in the following amounts:

Receivables, past due and not impaired	Gross amount as of 12/31/07	Receivables, past due, impaired	Receivables not impaired, past due, by period				
€ million			less than 30 days	31 to 60 days	61 to 90 days	91 to 120 days	over 120 days
Financial receivables	3,305	13	1		1		5
Trade accounts receivable	9,401	843	737	70	26	13	161
Other receivables and other assets	6,973	4	7				1
	19,679	**860**	**745**	**70**	**27**	**13**	**167**

Receivables, past due and not impaired € million	Gross amount as of 12/31/06	Receivables, past due, impaired	Receivables not impaired, past due, by period				
			less than 30 days	31 to 60 days	61 to 90 days	91 to 120 days	over 120 days
Financial receivables	4,554	6					
Trade accounts receivable	9,467	911	533	69	38	27	161
Other receivables and other assets	6,879	8	3				2
	20,900	**925**	**536**	**69**	**38**	**27**	**163**

Financial assets and liabilities can be broken down into categories with the following carrying amounts:

Carrying amounts by category € million	12/31/07	12/31/06
Financial assets recognized at fair value through profit or loss	5,418	5,398
of which: held for trading	(5,418)	(5,398)
Financial assets available for sale	11,869	18,472
Loans and receivables	14,197	16,698
Financial liabilities recognized at fair value through profit or loss	5,289	5,328
of which: held for trading	(5,289)	(5,328)
Financial liabilities carried at (amortized) cost	19,182	24,459

The following net results from financial instruments (as per IFRS 7) were recognized in the income statement:

Net gain/loss on financial instruments (IFRS 7) € million	2007	2006
Financial assets and liabilities recognized at fair value through profit or loss	434	-109
of which: held for trading	(434)	(-109)
Financial assets available for sale	753	919
Loans and receivables	-259	1,792
Financial liabilities carried at (amortized) cost	-991	-2,922

The net result (as per IFRS 7) includes interest, dividends and results from the measurement of financial instruments at fair value.

As a utility enterprise with international operations, the RWE Group is exposed to credit, liquidity and market risks in its ordinary business activity. In particular, market risks stem from changes in commodity prices, exchange rates, interest rates and share prices.

These risks are limited via systematic risk management. Among other things, risks are mitigated through hedges. RWE Group companies are also subjected to strict risk management. Binding internal directives define the range of action, responsibilities and controls.

Derivative financial instruments are used to hedge currency, commodity and interest rate risks from operations as well as risks from cash investments and financing transactions. The instruments most commonly used are foreign exchange forwards and options, interest rate swaps, interest rate currency swaps, and commodity forwards, options, futures and swaps. Additionally, derivatives may be used for proprietary trading purposes within defined limits.

Detailed information on the risks to which the RWE Group is exposed and on the objectives and procedures of the risk management is presented in the chapter "Development of opportunities and risks" in the review of operations.

Hedge accounting pursuant to IAS 39 is applied primarily for hedges of currency risks from net investments in foreign entities with foreign functional currencies, for hedges of foreign-currency liabilities and interest rate risks from non-current liabilities, as well as for hedging price risks from sales and purchase transactions.

Fair value hedges are mainly used to hedge fixed-interest loans and liabilities against market price risks. The objective of the hedge is to transform fixed-interest instruments into variable-rate instruments, thereby hedging their fair value. Instruments used are interest rate swaps and interest rate currency swaps. In the case of fair value hedges, both the derivative as well as the underlying transaction regarding the hedged risk are measured at fair value with an effect on income. As of the reporting date, the fair value of instruments used as fair value hedges amounted to -€25 million (previous year: -€35 million).

In the year under review, a loss of €2 million (previous year: gain of €51 million) was recognized in the financial result from adjustment of the carrying amount of the underlying transactions; a gain of €0 million (previous year: loss of €51 million) stemming from changes in the fair value of the hedges was recognized in the financial result.

Cash flow hedges exist primarily to hedge against foreign currency and price risks from future sales and purchase transactions. Hedging instruments consist of foreign exchange forwards and options, and commodity forwards, options, futures and swaps. Changes in the fair value of the hedges are disclosed under other comprehensive income until the underlying transaction is realized. The hedge's contribution to income is transferred from other comprehensive income to the income statement when the underlying transaction is realized. As of the reporting date, the recognized fair value of instruments used as cash flow hedges amounted to €426 million (previous year: -€677 million).

The future sales and purchase transactions hedged by cash flow hedges are expected to be realized in the following five years.

During the year under review, the ineffective portions of cash flow hedges amounted to €14 million (previous year: -€10 million), which was recognized with an effect on income.

Hedges of net investment in a foreign entity are used to hedge against the foreign currency risks of net investment in foreign entities with foreign functional currencies. Bonds with various terms in the appropriate currency and interest rate currency swaps are used as hedging instruments. Exchange rate changes from bonds used for hedging purposes and changes in the fair value of interest rate currency swaps are recognized under foreign currency translation adjustments in other comprehensive income. As of the reporting date, the fair value of instruments used to hedge net investment in foreign entities amounted to €2,548 million (previous year: €3,486 million).

During the year under review, the ineffective portions of hedges of net investment in foreign entities amounted to €36 million (previous year: €0 million), which was recognized with an effect on income.

Market risks result from fluctuations in prices on financial markets. Changes in exchange rates, interest rates and share prices can have an influence on the Group's results on operating activities. Due to the Group's international profile, exchange rate management is a key issue. The British pound and the US dollar are the two most important foreign currencies for two main reasons: On the one hand, the Group is engaged in business activities in these two currency zones. On the other hand, fuels are traded in these currencies. Group companies are generally required to hedge all currency risks via RWE AG, which determines the net financial position for each currency and hedges it with external market partners if necessary.

Interest rate risks stem primarily from financial debt and the Group's interest-bearing investments. Negative changes in value caused by unexpected interest-rate movements are hedged with non-derivative and derivative financial instruments.

Opportunities and risks from changes in the values of securities are controlled by a professional fund management system. The Group's financial transactions are recorded using centralized risk management software and monitored by RWE AG. This enables the balancing of risks across individual companies.

Group risk management has established directives for commodity operations, stipulating that derivatives may be used to hedge against price risks, optimize power plant schedules and increase margins. Furthermore, commodity derivatives may be traded, subject to strict limits. These limits are defined by independent organizational units and monitored on a daily basis.

All derivative financial instruments are recognized as assets or liabilities and are measured at fair value. When interpreting the positive and negative fair values of derivative financial instruments, with the exception of the relatively low commodity trading volumes, it must be taken into account that they are generally matched with underlying transactions that carry offsetting risks.

Maturities of interest rate, currency, share price or index-related and commodity derivatives are based on the maturities of the underlying transactions and are thus primarily short-term and medium-term in nature. Maturities of up to 30 years have been agreed upon to hedge foreign currency risks of foreign investments.

The Value-at-Risk method is used to quantify the interest rate, foreign currency and share-price risks for financial instruments as well as commodity price risks, in line with the international banking standard. The maximum expected loss arising from changes in market prices is calculated on the basis of historical market volatility and is monitored continuously.

The following Value-at-Risk information relates exclusively to recognized financial instruments, in line with the mandatory rules of IFRS 7. Off-balance-sheet planned positions which are hedged and so-called executory contracts in commodities may not be taken into account. As a result, an incomplete picture of the risk situation of the RWE Group is presented.

Value at Risk for financial derivatives € million	Value at Risk	
	12/31/07	12/31/06
Foreign currency derivatives	43.9	22.7
Forwards	5.3	5.7
Options	0.1	0.9
Interest rate currency derivatives	44.8	25.4
Interest rate derivatives	5.8	3.4
Share-price/index-related derivatives		1.9

As of December 31, 2007, the foreign currency Value at Risk for all items to be taken into account pursuant to IFRS 7 amounted to €17.2 million (previous year: €10.9 million). In accordance with IFRS 7, underlying transactions which are the subject of a cash flow hedge were not taken into consideration in determining this position. The Value at Risk determined in this manner thus represents a slightly pessimistic scenario, taking into account risk aspects.

As of December 31, 2007, the interest rate Value at Risk from financial debts and related hedging transactions amounted to €69.3 million (previous year: €34.5 million). Taking into account the hedges, the value at risk from interest-bearing assets amounted to €21.2 million (previous year: €18.8 million).

Share price Value at Risk was €17.3 million as of December 31, 2007 (previous year: €24.8 million).

As of December 31, 2007, commodity price Value at Risk pursuant to IFRS 7 amounted to €35.2 million (previous year: €97.6 million).

The Value-at-Risk figures are based on a confidence interval of 95% and a holding period of one day.

Credit risks. In our financial and trading operations, credit relationships mainly exist with banks and other trading partners with good creditworthiness. Credit risks associated with contractual partners are reviewed upon conclusion of the contract and constantly monitored. We also limit credit risk by the definition of limits for trading with contractual partners and through the use of cash collaterals. Credit insurance and bank guarantees are also employed. Credit risk in trading operations is monitored on a daily basis, and on a weekly basis for financial operations.

We are exposed to credit risks in our supply business, because it is possible that customers will fail to meet their financial obligations. This risk is mitigated by regular analysis of the creditworthiness of our customer portfolio based on the RWE Group’s credit risk directive.

The maximum default risk is expressed by the carrying value of the financial receivables stated in the balance sheet. The default risks for derivatives correspond to their positive fair values. Defaults in the year under review and the previous year were negligible.

Liquidity risks. As a rule, RWE AG centrally handles refinancing for RWE Group companies. In this regard, there is a risk that liquidity reserves will prove to be insufficient to meet financial obligations in a timely manner. In 2008, capital market debt with a nominal volume of approximately €1.6 billion and bank debt of €0.9 billion are due; additionally, short-term debt is also due. Liquidity needs are covered with cash and cash equivalents, and current marketable securities totalling €12,780 million. Above and beyond this, RWE AG has a fully committed, unused syndicated credit line of €4 billion. There are also unused reserves of €8.9 billion from the €20 billion debt issuance programme. Accordingly, liquidity risk is extremely low.

The financial liabilities are expected to result in the following (undiscounted) payments in the coming years:

Redemption and interest payments on financial liabilities € million	Carrying amount 12/31/07	Redemption payments			Interest payments		
		2008	2009 to 2012	From 2013	2008	2009 to 2012	From 2013
Bonds payable (incl. other notes payable)	10,651	1,623	2,703	6,403	604	2,019	3,402
Bank debt	1,354	913	316	125	18	45	19
Liabilities arising from finance lease agreements	146	13	43	90	4	14	9
Other financial liabilities	730	459	39	278	11	36	19
Derivative financial liabilities	6,078	4,700	-1,437	3	20	31	125
Collaterals for trading activities	404	404					
Miscellaneous other financial liabilities	8,753	8,697	44	49			

Redemption and interest payments on financial liabilities € million	Carrying amount 12/31/06	Redemption payments			Interest payments		
		2007	2008 to 2011	From 2012	2007	2008 to 2011	From 2012
Bonds payable (incl. other notes payable)	16,380	2,252	2,807	11,605	888	2,954	4,743
Commercial paper	546	546			14		
Bank debt	1,382	717	458	212	36	76	28
Liabilities arising from finance lease agreements	162	10	42	110	5	18	15
Other financial liabilities	740	529	63	196	10	29	27
Derivative financial liabilities	6,977	-13,061	-7,309	-101	10	34	168
Collaterals for trading activities	172	172					
Miscellaneous other financial liabilities	8,853	8,829	35	57			

(31) Contingent liabilities and financial commitments

Contingent liabilities € million	12/31/07	12/31/06
Contingent liabilities from general, draft and check guarantees		1
Contingent liabilities from granting collateral to third-party liabilities		10
Contingent liabilities from surety bonds	50	33
Contingent liabilities from other contingencies		4
	50	**48**

As of December 31, 2007, the Group had €2,073 million in capital commitments (previous year: €2,193 million). Moreover, assurances regarding acquisitions of investments existed in the amount of €129 million (previous year: €524 million).

RWE granted Rütgerswerke mbh, a subsidiary of RAG AG, a €400 million line of credit at fair market conditions, which was available until June 29, 2007. This line of credit was not used.

Commitments from operating leases refer largely to long-term rental arrangements for power generation and supply plants as well as rent and lease contracts for storage and administration buildings.

Minimum lease payments have the following maturity structure:

Operating leases € million	Nominal value	
	12/31/07	12/31/06
Due within one year	77	79
Due within one to five years	193	228
Due after five years	259	221
	529	**528**

Payment obligations for non-current financial assets amounted to €2 million (previous year: €2 million).

The RWE Power Division has entered into long-term purchase and service agreements for uranium, conversion, enrichment, production and waste management.

RWE bears customary commercial liability for long-term contracts in the plant construction business.

We bear the legal and contractual liability from our membership in various associations which exist in connection with power plant projects, profit- and loss-pooling agreements and for the provision of liability cover for nuclear risks, amongst others.

By signing a mutual benefit agreement, RWE AG and other parent companies of German nuclear power plant operators undertook to provide €2,244 million in funding to liable nuclear power plant operators to ensure that they are able to meet their payment obligations in the event of nuclear damages. RWE AG has a 25.851% contractual share in the liability, plus 5% for damage settlement costs.

RWE Group companies are involved in litigation and arbitration proceedings connected with their operations. However, RWE does not expect any material negative repercussions from these proceedings on the RWE Group's economic or financial position. Additionally, companies belonging to the RWE Energy Division are directly involved in various administrative and regulatory proceedings (including approval procedures) or are directly affected by their results.

Outside shareholders initiated several legal proceedings to examine the appropriateness of the conversion ratios and the amount of cash paid in compensation in connection with company restructurings pursuant to German company law. We are convinced that the conversion ratios and cash compensation calculated on the basis of expert opinions and verified by auditors are adequate. If the legally enforceable decisions come up with a different result, the compensation will be carried out by making an additional cash payment to the affected shareholders, including those who are not involved in the conciliation proceedings.

The EU Commission conducted follow-up inquiries at several European power utilities in May and December of 2006. This also affected RWE Group companies in Germany. Afterwards, the EU Commission filed requests with companies including RWE for information on individual energy market issues, which it will process further.

The EU Commission initiated an abuse procedure against RWE in early May 2007. It suspects that RWE hindered access to the natural gas transmission system in Germany in order to attain a purportedly market-dominating position in the gas supply business. This allegation primarily affects RWE Transportnetz Gas, a subsidiary of RWE Energy. However, the Commission expressly points out that the initiation of this procedure does not mean that it has conclusive evidence of any wrongdoing by RWE.

(32) Segment reporting

In the RWE Group, segments are distinguished on the basis of the services provided by the Group's divisions. The segmentation of divisions and geographical regions is based on the internal reporting system.

RWE Power is the segment comprising the entire Continental European power generation business as well as the Group's lignite production business. This segment also includes the upstream operations of RWE Dea (gas and oil production). The trading activities of RWE Trading are also reported in the segment RWE Power, in reflection of the closely intertwined business activities of these two divisions.

RWE Energy is the segment comprising distribution, transmission and sales for the Continental European electricity and gas businesses as well as substantial parts of the Continental water business. The new company RWE Gas Midstream GmbH, established in fiscal 2007, is also a part of the segment RWE Energy. This company is aligned to handle the commercial optimization of our non-regulated gas activities, including procurement, transport and storage contracts, as well as the liquefied natural gas (LNG) business.

RWE npower is a separate segment which covers all of the UK electricity and gas activities.

The Water Division, which primarily consists of the water business outside of Continental Europe, is reported separately as a discontinued operation in fiscal 2007 and 2006. In 2006, discontinued operations also included the RWE Thames Water Group, which was sold in 2006.

Consolidation effects and the Group Centre are disclosed under "Other/consolidation" as well as other activities not allocable to the divisions presented separately, primarily consisting of the shared services provided by RWE Systems.

Segment reporting Divisions 2007 € million	RWE Power	RWE Energy	RWE npower	Other/ consoli- dation	RWE Group	Water Division (discon- tinued operation)	RWE Group incl. Water Division
External revenue	**6,595**	**26,900**	**8,920**	**92**	**42,507**	**1,601**	**44,108**
Intra-group revenue	10,003	1,310	5	-11,318			
Total revenue	16,598	28,210	8,925	-11,226	42,507	1,601	44,108
Operating result	**3,706**	**2,296**	**724**	**-206**	**6,520**	**409**	**6,929**
Operating income from investments	69	460	3	9	541	-4	537
Operating income from investments accounted for using the equity method	44	380	3		427	-4	423
Operating depreciation and amortization	789	906	149	79	1,923	256	2,179
Total impairment losses	79	7		4	90		90
EBITDA	**4,426**	**2,742**	**870**	**-136**	**7,902**	**669**	**8,571**
Cash flows from operating activities	**2,531**	**1,809**	**592**	**1,153**[1]	**6,085**		
Capital employed (as per the value management concept)	15,349	20,844	6,424	-2,907	39,710		
Carrying amount of investments accounted for using the equity method	189	2,230	2		2,421		
Capital expenditure on intangible assets, property, plant and equipment and investment property	1,635	1,147	587	696[2]	4,065		

1 Of which American Water: € 526 million.
2 Of which American Water: € 635 million.

Regions 2007 € million	EU			Rest of Europe	America	Other	RWE Group
	Germany	UK	Other EU				
External revenue	24,840	9,555	6,840	1,015	8	249	42,507
Intangible assets, property, plant and equipment and investment property	17,451	8,089	5,848	505		180	32,073
Capital expenditure on intangible assets, property, plant and equipment and investment property	1,973	689	412	149	635	207	4,065

Segment reporting Divisions 2006 € million	RWE Power	RWE Energy	RWE npower	Water Division (discontinued operation)[1]	Other/ consolidation	RWE Group	Water Division (discontinued operation)	RWE Group[2]	RWE Thames Water (discontinued operation)	RWE Group incl. Water Division and RWE Thames Water
External revenue	**6,574**	**27,398**	**8,485**		**97**	**42,554**	**1,702**	**44,256**	**2,278**	**46,534**
Intra-group revenue	8,531	748	8		-9,287					
Total revenue	15,105	28,146	8,493		-9,190	42,554	1,702	44,256	2,278	46,534
Operating result	**2,744**	**2,506**	**512**		**-81**	**5,681**	**425**	**6,106**	**711**	**6,817**
Operating income from investments	115	261	4		6	386		386	6	392
Operating income from investments accounted for using the equity method	99	211	3			313	-1	312	4	316
Operating depreciation and amortization	743	932	150		52	1,877	264	2,141	401	2,542
Total impairment losses	29	70	10		6	115	11	126		126
EBITDA	**3,372**	**3,177**	**658**		**-35**	**7,172**	**689**	**7,861**	**1,106**	**8,967**
Cash flows from operating activities	**1,985**	**2,580**	**232**	**1,419**[3]	**567**	**6,783**				
Capital employed (as per the value management concept)	14,928	21,327	6,643		-2,692	40,206				
Carrying amount of investments accounted for using the equity method	184	2,085	1		1	2,271				
Capital expenditure on intangible assets, property, plant and equipment and investment property	1,302	1,174	396	1,584[4]	38	4,494				

1 In accordance with IFRS 5 the prior-year figures in the income statement were adjusted; the prior-year figures in the balance sheet, however, were not adjusted.
2 Prior to adjustment; as reported in the 2006 Annual Report.
3 Of which Thames Water: € 1,050 million.
4 Of which Thames Water: € 958 million.

Regions 2006	EU			Rest of Europe	America	Other	RWE Group
€ million	Germany	UK	Other EU				
External revenue	26,607	8,964	5,971	526	69	417	42,554
Intangible assets, property, plant and equipment and investment property	16,628	8,871	5,791	390	9,370	110	41,160
Capital expenditure on intangible assets, property, plant and equipment and investment property	1,730	1,523	393	82	626	140	4,494

Products € million	RWE Group	
	2007	2006
External revenue	42,507	42,554
of which: electricity	(27,917)	(25,771)
of which: gas	(10,768)	(12,055)
of which: crude oil	(1,023)	(1,255)

Notes on segment data. Intra-group revenue reflects the level of revenue between segments and is settled at arm's length conditions.

The definition of the operating result and capital employed is derived from the value management concept. Both of these indicators are used for control purposes within the group (cf. pages 208 et seq.). A reconciliation of the operating result to income from continuing operations before tax is presented below:

€ million	2007	2006
Operating result	**6,520**	**5,681**
Non-operating result	-149	-330
Financial result	-1,138	-1,814
Income from continuing operations before tax	**5,233**	**3,537**

Income and expenses that are unusual from an economic perspective, or are the result of exceptional events, prejudice the assessment of operating activities. They are reclassified to the non-operating result. In the event that impairment losses are recognized on goodwill of fully consolidated companies, such losses are contained in the non-operating result.

More detailed information is presented on pages 73 to 74 in the review of operations.

Capital expenditure includes spending on intangible assets, property, plant and equipment and investment property.

RWE did not generate more than 10% of sales revenues with any single customer in the year under review or the previous year.

(33) Notes to the cash flow statement

The cash flow statement classifies cash flows according to operating, investing and financing activities. Cash and cash equivalents in the cash flow statement correspond to total cash and cash equivalents on the balance sheet. Cash and cash equivalents consist of cash on hand, demand deposits and fixed-interest marketable securities with a maturity of three months or less from the date of acquisition.

Flows of funds from the acquisition and sale of consolidated companies are included in cash flows from investing activities. Effects of foreign exchange rate changes are stated separately.

Among other things, cash flows from operating activities include:

- cash flows from interest income of €861 million (previous year: €2,048 million) and cash flows used for interest expenses of €1,517 million (previous year: €2,827 million);
- €970 million (previous year: €998 million) in taxes on income paid (less income tax refunds); and
- cash flows from investments (dividends) amounting to €372 million (previous year: €485 million), net of the portion stemming from accounting using the equity method that does not have an effect on cash flows.

Cash flows from financing activities include €1,968 million (previous year: €984 million) which was paid out to RWE shareholders and €231 million (previous year: €224 million) which was distributed to minority shareholders. New issuance of financial debt totalled €5,577 million (previous year: €7,526 million) and was contrasted by repayments of €5,822 million (previous year: €9,257 million).

Changes in the scope of consolidation resulted in a net change in cash and cash equivalents of -€21 million (previous year: -€996 million).

Cash and cash equivalents of €7 million (previous year: €0 million) stemming from acquisitions are offset against capital expenditure on financial assets. Divested cash and cash equivalents of €28 million (previous year: €996 million) are included in proceeds from divestitures.

Exploration activities resulted in cash flows from operating activities in the amount of -€150 million (previous year: -€110 million) and cash flows from investing activities of -€221 million (previous year: -€101 million).

In the year under review, the variation margins, which were reported in previous years under collaterals for trading activities, were netted out against the market values of the underlying derivatives. Payments from variation margins are now stated in cash flows from operating activities, and not in cash flows from financing activities. €471 million of the variation margins reported in cash flows from operating activities are related to derivatives which are used in cash flow hedges.

First-time consolidations and deconsolidations resulted in an increase of €44 million in net financial debt.

There are no restrictions on the disposal of cash and cash equivalents.

Net debt of the RWE Group € million	12/31/07	12/31/06
Cash and cash equivalents	1,922	2,794
Marketable securities	10,858	16,788
Non-current marketable securities	444	1,047
Collaterals for trading activities	1,118	2,426
Other financial receivables	1,007	1,047
Financial assets	**15,349**	**24,102**
Bonds, other notes payable, bank debt, commercial paper	12,005	18,308
Collaterals for trading activities	404	172
Other financial liabilities	876	902
Financial liabilities	**13,285**	**19,382**
Net financial debt from continuing operations	**-2,064**	**-4,720**
Provisions for pensions and similar obligations	3,496	11,584
Net debt from continuing operations	**1,432**	**6,864**
Net debt from discontinued operations	3,624	
Net debt of the RWE Group	**5,056**	**6,864**

Other financial receivables essentially consist of other loans, deferred interest, and financial receivables from non-consolidated subsidiaries and investments. Other financial debt essentially includes financial liabilities to non-consolidated subsidiaries and investments, as well as miscellaneous other financial liabilities. Net financial debt is the difference between financial assets and financial liabilities.

(34) Information on concessions

A number of easement agreements and concession contracts have been concluded in the fields of electricity, gas and water between RWE Group companies and governmental authorities in the areas supplied by RWE.

Easement agreements are used in the electricity and gas business to regulate the use of public rights of way for laying and using lines for public energy supply. These agreements are limited to a term of 20 years. When the agreements expire, there is a legal obligation to transfer ownership of the local distribution facilities to the new energy supplier, in exchange for appropriate compensation of RWE.

Water concession agreements contain provisions for the right and obligation to provide water and wastewater services, operate the associated infrastructure, such as water utility plants, as well as to implement capital expenditure. Concessions in the water business generally have terms of up to 50 years.

(35) Related party disclosures

Within the framework of their ordinary business activities, RWE AG and its subsidiaries have business relationships with numerous companies. These include associates, which are classified as parties related to the Group, along with the RWE Energy Division's investments in municipal enterprises accounted for using the equity method, especially municipal utilities.

In the 2007 fiscal year, business transactions concluded with major related parties led to the following items in RWE's consolidated financial statements:

Key items from transactions with associates € million	2007	2006
Revenue	566	938
Expenses	87	125
Receivables	814	951
Liabilities	4	86

All business transactions are completed at arm's length prices and on principle do not differ from the conditions for supply and services provided to other enterprises.
€88 million of the receivables (previous year: €232 million) and €4 million of the liabilities (previous year: €86 million) fall due within one year. In respect of the receivables there are guarantees of €0 million, as in the previous year, and other collaterals amounting to €1 million (previous year: €4 million). The receivables include €725 million in interest-bearing loans to the Berlinwasser Group (previous year: €720 million).

Above and beyond this, as of December 31, 2007, there was an unused €25 million line of credit for the Berlinwasser Group (previous year: €30 million).

Furthermore, since October 1, 2007, the companies of the Georgsmarienhütte Group are now classified as related companies, as the CEO of RWE AG, Dr. Großmann, is a partner in Georgsmarienhütte Holding GmbH. Since October 1, 2007, RWE Group companies have provided services and deliveries amounting to €2 million to companies of the Georgsmarienhütte Group. Since October 1, 2007, companies belonging to the Georgsmarienhütte Group have provided services and deliveries amounting to €0.1 million to RWE Group companies. As of December 31, 2007, the Georgsmarienhütte Group had liabilities of €0.7 million to RWE Group companies. All business transactions are completed at arm's length prices and on principle do not differ from the conditions for supply and services provided to other enterprises.

No material business transactions were concluded between the RWE Group and related persons.

The compensation model and compensation of the Executive and Supervisory Boards is presented in the compensation report, which is included in the review of operations.

In total, the compensation of the Executive Board amounted to €17,376,000 (previous year: €18,038,000), plus pension service costs of €1,913,000 (previous year: €1,954,000). The Executive Board received short-term compensation components amounting to €12,782,000 in fiscal 2007. In addition to this, long-term compensation components from the 2007 tranche of the Beat programme in the amount of €4,594,000 were allocated.

The Supervisory Board received total compensation of €3,237,000 (previous year: €3,481,000) in fiscal 2007. Supervisory Board members also received €268,000 in compensation from subsidiaries for the exercise of mandates (previous year: €194,000).

Former members of the Executive Board and their surviving dependents received €8,932,000 (previous year: €11,803,000), of which €1,899,000 came from subsidiaries (previous year: €1,885,000). LTIP options were not exercised (previous year: €2,787,000). The total amount also includes compensation of €38,000 from subsidiaries for the exercise of mandates. As of the balance-sheet date, €114,729,000 (previous year: €111,291,000) has been accrued for defined benefit obligations to former members of the Executive Board and their surviving dependents, of which €19,344,000 was set aside at subsidiaries (previous year: €23,672,000).

The Economic Advisory Board was paid total compensation of €289,000 (previous year: €363,000, including compensation of €36,000 for mandates at subsidiaries).

Declarations on the members of the Executive and Supervisory Boards in accordance with Sec. 285 No. 10 of the German Commercial Code (HGB) are presented on pages 210 to 214.

(36) Auditor's fees

The following fees were recognized as expenses for the services rendered in fiscal 2007 and in the prior year by the auditors of the consolidated financial statements, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft and companies belonging to PwC's international network:

Auditor's fees	2007		2006	
€ million	Total	Of which: Germany	Total	Of which: Germany
Audit services	17.6	9.3	16.7	7.3
Other assurance and valuation services	3.1	3.0	4.8	4.6
Tax services	0.4	0.2	1.8	0.8
Other services rendered for RWE AG or subsidiaries	0.6	0.5	0.3	0.3
	21.7	**13.0**	**23.6**	**13.0**

The total expenses include fees related to discontinued operations amounting to €4.3 million (previous year: €6.4 million).

The fees for audit services primarily contain the fees for the audit of the consolidated financial statements, review of the interim reports, and for the audit of the financial statements of RWE AG and its subsidiaries. Fees for other assurance or valuation services related principally to due diligence services in relation to acquisitions and disposals. This item also includes fees for review of the internal controlling system, in particular the IT systems and expenses related to statutory or court ordered requirements. Fees for tax services mainly include fees for consultation in relation to the preparation of tax returns and review of resolutions of the tax authorities as well as national and international tax-related matters. Up to October 31, 2006, they also include tax consultation for employees living abroad.

(37) Application of Sec. 264, Para. 3 and Sec. 264b of the German Commercial Code

The following German subsidiaries made use of the exemption clause included in Sec. 264, Para. 3 and Sec. 264b of the German Commercial Code:

- BGE Beteiligungs-Gesellschaft für Energieunternehmen mbH, Essen
- eprimo GmbH, Neu-Isenburg
- GBV Dreizehnte Gesellschaft für Beteiligungsverwaltung mbH & Co. KG, Essen
- GBV Fünfte Gesellschaft für Beteiligungsverwaltung mbH, Essen
- GBV Siebte Gesellschaft für Beteiligungsverwaltung mbH, Essen
- GBV Vierzehnte Gesellschaft für Beteiligungsverwaltung mbH, Essen
- HEC GmbH, Dortmund
- Kavernenspeicher Staßfurt GmbH, Staßfurt
- OIE Aktiengesellschaft, Idar-Oberstein
- Rheinische Baustoffwerke GmbH, Bergheim
- rhenag Beteiligungs GmbH, Cologne
- RWE Aqua Holdings GmbH, Essen
- RWE Aqua International GmbH, Essen
- RWE Dea AG, Hamburg
- RWE Dea Suez GmbH, Hamburg
- RWE Energy Aktiengesellschaft, Dortmund
- RWE Energy Beteiligungsgesellschaft mbH, Dortmund
- RWE Fuel Cells GmbH, Essen
- RWE Gas Midstream GmbH, Essen
- RWE KAC Dezentrale Energien GmbH & Co. KG, Dortmund
- RWE Key Account Contracting GmbH, Essen
- RWE Key Account GmbH, Essen
- RWE Kundenservice GmbH, Bochum
- RWE Plus Beteiligungsgesellschaft Mitte mbH, Essen
- RWE Power Aktiengesellschaft, Cologne and Essen
- RWE Power Erste Gesellschaft für Beteiligungsverwaltung mbH, Essen
- RWE Rhein-Ruhr Aktiengesellschaft, Essen
- RWE Rhein-Ruhr Netzservice GmbH, Siegen
- RWE Rhein-Ruhr Verteilnetz GmbH, Wesel
- RWE Rhenas Versicherungsvermittlung GmbH, Essen
- RWE Solutions Aktiengesellschaft, Alzenau
- RWE Systems Aktiengesellschaft, Dortmund
- RWE Systems Computing GmbH, Dortmund
- RWE Systems Consulting GmbH, Essen
- RWE Systems Development GmbH & Co. KG, Dortmund
- RWE Systems Immobilien Alzenau GmbH, Alzenau
- RWE Systems Immobilien GmbH u. Co. KG, Essen
- RWE Trading GmbH, Essen
- RWE Transportnetz Gas GmbH, Dortmund
- RWE Transportnetz Strom GmbH, Dortmund
- RWE Westfalen-Weser-Ems Aktiengesellschaft, Dortmund
- RWE Westfalen-Weser-Ems Netzservice GmbH, Dortmund
- RWE Westfalen-Weser-Ems Verteilnetz GmbH, Recklinghausen
- SKW Steinkohlen-Wärme GmbH, Kamp-Lintfort
- Thyssengas GmbH, Duisburg

(38) Declaration according to Sec. 161 of the German Stock Corporation Act

The declarations on the German Corporate Governance Code prescribed by Sec. 161 of the German Stock Corporation Act (AktG) have been submitted for RWE AG and its publicly traded subsidiaries and have been made accessible to the shareholders.

(39) Events after the balance-sheet date

Information on events after the balance-sheet date is presented in the review of operations.

4.6 Auditor's Report

We have audited the consolidated financial statements – comprising the income statement, the balance sheet, cash flow statement, statement of changes in equity and the notes to the consolidated financial statements – together with the review of operations of RWE Aktiengesellschaft, Essen, which is combined with the review of operations of the Company, for the business year from January 1 to December 31, 2007. The preparation of the consolidated financial statements and the combined review of operations in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315a Abs. (paragraph) 1 HGB ("Handelsgesetzbuch": "German Commercial Code") are the responsibility of the parent Company's Executive Board. Our responsibility is to express an opinion on the consolidated financial statements and the combined review of operations based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW) and additionally observed the International Standards on Auditing (ISA). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with (German) principles of proper accounting and in the combined review of operations are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the combined review of operations are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of the companies included in consolidation, the determination of the companies to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Executive Board, as well as evaluating the overall presentation of the consolidated financial statements and the combined review of operations. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit, the consolidated financial statements comply with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The combined review of operations is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Essen, Germany, 14 February 2008

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

Manfred Wiegand	Markus Dittmann
Wirtschaftsprüfer	Wirtschaftsprüfer
(German Public Auditor)	(German Public Auditor)

Material Investments as of December 31, 2007

I. Affiliates	Investment in acc. With Sec. 16 of the German Stock Corporation Act %	Equity of the last fiscal year €'000	Net income/ loss of the last fiscal year €'000	Revenue 2007 € million	Employees[2] 2007 average
RWE Aktiengesellschaft, Essen		**8,400,050**	**2,944,906**	**–**	**355**
RWE Power					
RWE Power Aktiengesellschaft, Cologne and Essen	100	2,171,058	-[1]	8,579	13,184
Kernkraftwerke Lippe-Ems GmbH, Lingen (Ems)	99	165,545	-[1]	267	303
Kernkraftwerk Gundremmingen GmbH, Gundremmingen	75	84,184	8,343	256	712
Mátrai Erömü Zártkörüen Müködö Részvénytársaság (MÁTRA), Visonta/Hungary	51	200,203	47,002	277	2,420
Rheinbraun Brennstoff GmbH, Cologne	100	63,294	-[1]	543	164
RWE Dea AG, Hamburg	100	1,323,905	-[1]	1,020	807
RWE Dea Norge AS, Oslo/Norway	100	153,201	54,506	251	59
RWE Dea Suez GmbH, Hamburg	100	87,226	-[1]	185	106
RWE Trading GmbH, Essen	100	51,100	-[1]	13,760	511
RWE Energy					
RWE Energy Aktiengesellschaft, Dortmund	100	1,017,905	-[1]	7,785	488
Budapesti Elektromos Müvek Nyrt. (ELMÜ), Budapest/Hungary	55	1,041,267	767,498	1,080	695
Emscher Lippe Energie GmbH, Gelsenkirchen	79	73,371	12,317	485	649
Energis GmbH, Saarbrücken	64	136,782	22,588	345	327
envia Mitteldeutsche Energie AG, Chemnitz	64	888,810	99,286	2,348	2,173
envia Netzservice GmbH, Chemnitz	100	4,045	-[1]	341	7
envia Verteilnetz GmbH, Halle (Saale)	100	24	-[1]	1,653	4
eprimo GmbH, Neu-Isenburg	100	4,600	-[1]	87	30
Észak-magyarországi Áramszolgáltató Nyrt. (ÉMÁSZ), Miskolc/Hungary	54	366,442	229,688	387	356
EWV Energie- und Wasser-Versorgung GmbH, Stolberg	54	36,457	11,261	349	370
Jihomoravská plynárenská, a.s., Brno/Czech Republic	50	205,446	24,540	595	945
Koblenzer Elektrizitätswerk und Verkehrs-Aktiengesellschaft, Koblenz	58	71,793	5,539	412	532
Lechwerke AG, Augsburg	90	226,756	53,150	883	1,142
LEW Verteilnetz GmbH, Augsburg	100	25	-[1]	530	4
MITGAS Mitteldeutsche Gasversorgung GmbH, Halle	60	93,786	25,004	677	293
rhenag Rheinische Energie Aktiengesellschaft, Cologne	75	278,434	164,192	267	325
RWE Energy Beteiligungsgesellschaft mbH, Dortmund	100	4,350,032	-[1]	–	–
RWE Energy Nederland N.V., Hoofddorp/Netherlands	100	368,240	35,730	1,198	166
RWE Gas International B.V., Hoofddorp/Netherlands	100	4,507,949	241,407	–	–
RWE Key Account GmbH, Essen	100	25	-[1]	1,999	98
RWE Kundenservice GmbH, Bochum	100	25	-[1]	260	14
RWE Obragas N.V., Helmond/Netherlands	100	99,211	20,643	240	78

1 Profit- and loss-pooling agreement.
2 Converted to full-time positions.

Material Investments

as of December 31, 2007

I. Affiliates	Investment in acc. With Sec. 16 of the German Stock Corporation Act %	Equity of the last fiscal year €'000	Net income/ loss of the last fiscal year €'000	Revenue 2007 € million	Employees[3] 2007 average
RWE Energy					
RWE Rhein-Ruhr Aktiengesellschaft, Essen	100	238,405	-[1]	5,114	4,816
RWE Rhein-Ruhr Netzservice GmbH, Siegen	100	25	-[1]	704	30
RWE Rhein-Ruhr Verteilnetz GmbH, Wesel	100	25	-[1]	2,241	6
RWE Stoen S.A., Warschau/Poland	100	190,384	15,042	516	919
RWE Transgas, a.s., Prag/Czech Republic	100	3,465,323	461,602	2,579	315
RWE Trangas Net, s.r.o., Prag/Czech Republic	100	2,054,020	243,586	369	710
RWE Transportnetz Gas GmbH, Dortmund	100	55	-[1]	299	76
RWE Transportnetz Strom GmbH, Dortmund	100	613,025	-[1]	4,860	276
RWE Westfalen-Weser-Ems Aktiengesellschaft, Dortmund	80	283,185	-[1]	4,784	2,646
RWE Westfalen-Weser-Ems Netzservice GmbH, Dortmund	100	25	-[1]	912	23
RWE Westfalen-Weser-Ems Verteilnetz GmbH, Recklinghausen	100	25	-[1]	1,663	3
RWW Rheinisch-Westfälische Wasserwerksgesellschaft mbH, Mülheim an der Ruhr	80	74,690	8,433	106	433
Severočeská plynárenská, a.s., Ústí nad Labem/Czech Republic	100	117,107	20,226	308	380
Severomoravská plynárenská, a.s., Ostrava/Czech Republic	68	190,149	36,655	442	640
Stadtwerke Düren GmbH, Düren	75	27,044	6,312	155	214
Středočeská plynárenská, a.s., Prag/Czech Republic	97	92,267	2,270	258	366
Süwag Energie AG, Frankfurt am Main	78	264,359	44,050	1,501	1,441
Süwag Netz GmbH, Frankfurt am Main	100	25	-[1]	481	13
Thyssengas GmbH, Duisburg	100	179,695	-[1]	101	–
VSE Aktiengesellschaft, Saarbrücken	69	133,212	14,301	327	297
Východočeská plynárenská, a.s., Hradec Králové/Czech Republic	67	121,360	16,373	269	461
Západočeská plynárenská, a.s., Plzen/Czech Republic	100	99,893	24,030	201	343
RWE npower					
RWE Npower Holdings plc, Swindon/UK[2]	100	940,138	216,912	8,925	11,845
Water Division					
American Water Works Company, Inc., Wilmington/Delaware/USA American Water-Group[2,4] with 65 subsidiaries in the US and Canada	100	3,801,662	- 117,592	1,601	5,257
Other subsidiaries					
RWE Finance B.V., Hoofddorp/Netherlands	100	10,309	4,214	–	–
RWE Systems Aktiengesellschaft, Dortmund	100	275,775	-[1]	2,009	1,506

1 Profit- and loss-pooling agreement.
2 Figures from the company's financial statements.
3 Converted to full-time positions
4 Discontinued operation.

II. Companies accounted for using the equity method	Investment in acc. with Sec. 16 of the German Stock Corporation Act %	Equity of the last fiscal year €'000	Net income/ loss of the last fiscal year €'000
RWE Power			
TCP Petcoke Corporation, Dover/Delaware/USA[1]	50	5,649	10,607
Grosskraftwerk Mannheim Aktiengesellschaft, Mannheim	40	114,141	6,647
RWE Energy			
AVU Aktiengesellschaft für Versorgungs-Unternehmen, Gevelsberg	50	62,965	14,436
Cegedel S.A., Luxemburg/Luxembourg[1]	30	488,450	75,286
Dortmunder Energie- und Wasserversorgung GmbH (DEW 21), Dortmund	47	150,437	65,406
EVH GmbH, Halle (Saale)	30	76,736	236
Fövárosi Gázmüvek Zrt., Budapest/Hungary	50	162,886	20,765
Kärntner Energieholding Beteiligungs-GmbH, Klagenfurt/Austria[1]	49	418,262	31,470
KEW Kommunale Energie- und Wasserversorgung AG, Neunkirchen	29	71,171	8,533
Niederrheinische Versorgung und Verkehr Aktiengesellschaft, Mönchengladbach[1]	50	437,706	32,558
Pfalzwerke Aktiengesellschaft, Ludwigshafen	27	186,256	19,089
Regionalgas Euskirchen GmbH & Co. KG, Euskirchen	43	48,803	9,297
RheinEnergie AG, Cologne	20	564,045	185,358
RWE-Veolia Berlinwasser Beteiligungs AG, Berlin	50	275,854	11,925
SpreeGas Gesellschaft für Gasversorgung und Energiedienstleistung mbH, Cottbus	33	21,044	6,616
Stadtwerke Duisburg Aktiengesellschaft, Duisburg	20	153,223	26,543
Stadtwerke Essen Aktiengesellschaft, Essen	29	116,557	33,945
Südwestfalen Energie und Wasser AG, Hagen	19	277,865	13,261
TIGÁZ Tiszántúli Gázszolgáltató Zrt., Hajdúszoboszló/Hungary	44	141,190	- 2,854
Východoslovenská energetika, a.s., Košice/Slovakia	49	194,940	61,089
ZOV Zagrebacke Optpadne Vode d.o.o., Zagreb/Croatia	49	81,835	29,863

1 Figures from the company's financial statements.

III. Other Investments	Investment in acc. With Sec. 16 of the German Stock Corporation Act %	Equity of the last fiscal year €'000	Net income/ loss of the last fiscal year €'000
RWE Energy			
Stadtwerke Chemnitz Aktiengesellschaft, Chemnitz	19	255,387	20,967

The RWE Group's value management

Return-oriented control of the company. Increasing shareholder value lies at the heart of our strategy. Additional value is created when the return on capital employed (ROCE) exceeds capital costs. ROCE reflects the pure operating return. It is calculated by dividing the operating result by capital employed.

We calculate our cost of capital as a weighted average cost of equity and debt. Equity capital costs cover the capital market's expectation of company-specific returns when investing in an RWE share over and above that of a risk-free investment. The cost of debt is linked to long-term financing conditions in the RWE Group and allows interest on debt to be classified as tax deductible (tax shield).

The table at the top of page 209 shows the parameters used to calculate capital costs. As of fiscal 2006, we adapted some of these parameters to developments on the market and business performance. We calculate the Group's cost of debt by applying a pre-tax cost rate of 5.25%. The cost of equity is derived on the basis of an interest rate of 4.75%, which is customary for a risk-free investment, plus risk charges specific to the Group and the Group's divisions. Here, we operate on the basis of a beta factor of 0.74. The ratio of equity to debt is 50:50. We do not derive this parameter from the amounts carried on the balance sheet, but, among other things, from the marked-to-market valuation of equity and assumptions concerning the long-term development of our net financial position and provisions. The RWE Group's cost of capital was thus 9.0% before tax, as in 2006.

Relative value added is the difference between ROCE and capital costs. Multiplying this figure by the capital employed results in the absolute value added, which we employ as a central management benchmark. The higher the value added, the more attractive a particular activity is for our portfolio. It is the most important criterion for evaluating capital expenditure and for determining bonus payments for RWE Group executives.

Change in methodology starting in 2007. We have modified the methodology underlying our value management concept. Depreciable non-current assets are no longer stated at carrying amounts. Instead, we recognize half of their historic costs. However, we still fully account for the goodwill included in the purchase price of financial assets. The return criteria we apply to our acquisition projects continue to be based on the book value concept.

The advantage of the new procedure is that the determination of ROCE is no longer influenced by the depreciation period. This reduces the fluctuation in return caused by the investment cycle. We applied the new concept in the financial year that just ended for the first time. To ensure comparability to prior-year figures, we adjusted them accordingly. Due to the switch in methodology, the RWE Group now states a much higher level of working capital and, accordingly, lower returns. The most significant deviations from the old concept occur in the RWE Power and RWE Energy Divisions.

Lower capital costs starting in 2008. We made a second adjustment to the value management concept, which concerns the level of capital costs. From 2008 onwards, we will reduce the cost of capital for the RWE Group by half a percentage point to 8.5%. We are reducing the level of capital costs for our divisions and the individual business units by half a percentage point as well. The cost of capital for RWE Dea will be lowered by a full percentage point. This is in light of the decrease in the corporate tax rates in Germany and the UK that was decided on for 2008. By adjusting the cost of capital before taxes, we ensure that the cost of capital after taxes will remain unchanged. It amounts to 6.0% for the RWE Group.

RWE Group-capital costs		2007	from 2008
Risk-free interest rate	%	4.75	4.75
Market premium	%	5.0	5.0
Beta factor		0.74	0.67
Cost of equity after tax	%	8.5	8.1
Cost of debt before tax	%	5.25	5.25
Tax rate for debt	%	31.4	27.0
Tax shield	%	-1.65	-1.40
Cost of debt after tax	%	3.6	3.8
Proportion of equity	%	50	50
Proportion of debt	%	50	50
Capital costs after tax	%	**6.0**	**6.0**
Tax rate for blanket conversion	%	35	30
Weighted average cost of capital (WACC) before tax	%	**9.0**	**8.5**

RWE Group-determining capital employed		12/31/2006	12/31/2007
Intangible assets/property, plant and equipment[1]	€ million	53,456	46,598
+ Inestments including loans	€ million	3,917	3,902
+ Inventories	€ million	2,226	2,352
+ Trade accounts receivable	€ million	8,871	8,812
+ Other accounts receivable and other assets[3]	€ million	8,855	8,874
- Non-interest-bearing provisions[4]	€ million	10,380	10,972
- Non-interest-bearing liabilities[5]	€ million	20,635	18,467
- Adjustments[6]	€ million	1,086	1,134
Capital employed	€ million	**45,224**	**39,965**

RWE Group-determining value added			2007
Capital employed before adjustments (averaged for the year)	€ million		42,595
- Adjustments[7]	€ million		2,885
Capital employed after adjustments (averaged for the year)	€ million		**39,710**
Operating result	€ million		**6,520**
+ Interest income from lease receivables	€ million		11
Operating result for calculating ROCE	€ million		**6,531**
ROCE	%		**16.4**
Relative value added	%		**7.4**
Absolute value added	€ million		**2,957**

1 Intangible assets; property, plant and equipment; and investment property were stated at cost (see the statement on changes in assets); goodwill and the customer base were recognized at carrying amounts.
2 Investments accounted for using the equity method and other financial assets (excluding non-current securities).
3 Including tax refund claims; excluding the net present value of defined contribution pension benefit obligations as well as derivative financial instruments in the amount of €424 million (previous year: €282 million).
4 Including tax provisions and other provisions; excluding non-current provisions in the amount of €581 million (previous year: €720 million).
5 Including trade liabilities, income tax liabilities and other liabilities; excluding derivative financial instruments in the amount of €282 million (previous year €248 million) and purchase price liabilities of €1,951 million (previous year: €1,936 million) from put options and a forward purchase of minority interests.
6 Assets capitalized in accordance with IAS 16.15 in the amount of €529 million (previous year: €424 million) are not taken into account since these assets do not employ capital. Deferred tax liabilities relating to RWE npower's capitalized customer base are not taken into account, either.
7 Corrected to account for first-time consolidations and deconsolidations during the year—among other things—and the statement of American Water as a discontinued operation.

Boards and Committees

Supervisory Board

Dr. Thomas R. Fischer
Berlin
Chairman
Banker
- Audi AG
- Hapag-Lloyd AG

Frank Bsirske
Berlin
Deputy Chairman
Chairman of ver.di
Vereinte Dienstleistungsgewerkschaft
- Deutsche Lufthansa AG
- IBM Central Holding GmbH
- KfW – Kreditanstalt für Wiederaufbau

Dr. Paul Achleitner
Munich
Member of the Board of Management of Allianz SE
- Allianz Deutschland AG
- Allianz Global Investors AG
- Allianz Lebensversicherungs-AG
- Bayer AG
- Allianz Elementar Versicherungs-AG (Chairman)
- Allianz Elementar Lebensversicherungs-AG (Chairman)

Sven Bergelin*
Berlin
– until August 15, 2007 –
General Manager for Energy at
ver.di Vereinte Dienstleistungsgewerkschaft
- E.ON AG
- E.ON Avacon AG

Werner Bischoff
Monheim am Rhein
Member of the Main Executive Board of
IG Bergbau, Chemie, Energie
- Continental AG
- Evonik-Degussa GmbH
- RWE Dea AG
- Sanofi-Aventis Deutschland GmbH
- Hoechst GmbH
- RWE Power AG
- BGAG Beteiligungsgesellschaft der Gewerkschaften GmbH
- THS TreuHandStelle für Bergmannswohnstätten im rheinisch-westfälischen Steinkohlenbezirk GmbH

Carl-Ludwig von Boehm-Bezing
Bad Soden
Former member of the Board of Management of
Deutsche Bank AG

Heinz Büchel
Trier
Chairman of the General Works Council of
RWE Rhein-Ruhr AG
- RWE Energy AG

Dieter Faust
Eschweiler
Chairman of the Works Council, Plant Services/
Materials Management of RWE Power AG

Simone Haupt
Hagen
Chairman of the General Works Council of
RWE Systems AG

- Member of other mandatory supervisory boards.
- Member of comparable domestic and foreign supervisory bodies of commercial enterprises.

* Information valid as of the date of retirement from the Supervisory Board.

Heinz-Eberhard Holl
Osnabrück
Former Chief Administrative Officer,
Osnabrück Rural District
- Georgsmarienhütte GmbH
- Georgsmarienhütte Holding GmbH

Dr. Gerhard Langemeyer
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Mayor of the City of Dortmund
- Dortmunder Stadtwerke AG (Chairman)
- Gesellschaft für Vermögensverwaltung AG
- KEB Holding AG (Chairman)
- Klinikum Dortmund gGmbH (Chairman)
- Schüchtermann Schiller'sche Kliniken KG
- Sparkasse Dortmund (Chairman)

Dagmar Mühlenfeld
Mülheim an der Ruhr
Mayor of the City of Mülheim an der Ruhr
- Mülheimer Wohnungsbau e.G. (Chairman)
- Beteiligungsholding Mülheim an der Ruhr GmbH
- Flughafen Essen/Mülheim GmbH (Chairman)
- medl GmbH (Chairman)
- Mülheim & Business GmbH (Chairman)
- Ruhrbania Projektentwicklungsgesellschaft mbH (Chairman)
- Ruhrgebiet Tourismus Management GmbH

Erich Reichertz
Mülheim an der Ruhr
Diploma in engineering
- RWE Energy AG

Dr. Wolfgang Reiniger
Essen
Mayor of the City of Essen
- EGZ Entwicklungsgesellschaft Zollverein mbH
- EMG Essen Marketing GmbH Gesellschaft für Stadtwerbung, Touristik und Zentrenmanagement (Chairman)
- Entwicklungsgesellschaft Universitätsviertel Essen mbH (Chairman)
- Essener Wirtschaftsförderungsgesellschaft mbH (Chairman)
- Margarethe Krupp-Stiftung für Wohnungsfürsorge (Chairman)
- Messe Essen GmbH (Chairman)
- Sparkasse Essen (Chairman)

Günter Reppien
Lingen
Chairman of the General Works Council of
RWE Power AG
- RWE Power AG
- Stadtwerke Lingen GmbH

Karl-Heinz Römer
Mülheim an der Ruhr
– since October 2, 2007 –
District General Manager of
ver.di Vereinte Dienstleistungsgewerkschaft
- RWE Energy AG
- RWE Rhein-Ruhr AG
- RWE Westfalen-Weser-Ems AG

Dagmar Schmeer
Saarbrücken
Chairman of the Works Council of VSE AG
- VSE AG

- Member of other mandatory supervisory boards.
- Member of comparable domestic and foreign supervisory bodies of commercial enterprises.

* Information valid as of the date of retirement from the Supervisory Board.

Dr. Manfred Schneider
Leverkusen
Chairman of the Supervisory Board of Bayer AG
- Daimler AG
- Linde AG (Chairman)
- Metro AG
- TUI AG

Dr.-Ing. Ekkehard D. Schulz
Krefeld
Chairman of the Executive Board of ThyssenKrupp AG
- AXA Konzern AG
- Bayer AG
- MAN AG
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- ThyssenKrupp Steel AG (Chairman)
- ThyssenKrupp Technologies AG (Chairman)

Uwe Tigges
Bochum
Chairman of the General Works Council of RWE Westfalen-Weser-Ems AG
- RWE Energy AG
- RWE Westfalen-Weser-Ems AG

Prof. Karel Van Miert
Beersel
Professor, Nyenrode University
- Münchener Rückversicherungs-Gesellschaft AG
- Agfa-Gevaert N.V.
- Anglo American plc
- De Persgroup
- Koninklijke Philips Electronics N.V.
- SIBELCO N.V.
- SOLVAY S.A.
- Vivendi Universal S.A.

▪ Member of other mandatory supervisory boards.
▪ Member of comparable domestic and foreign supervisory bodies of commercial enterprises.
* Information valid as of the date of retirement from the Supervisory Board.

Supervisory Board Committees

Executive Committee of the Supervisory Board

Dr. Thomas R. Fischer (Chairman)

Frank Bsirske

Dr. Paul Achleitner

Heinz Büchel

Dieter Faust

Simone Haupt

Dagmar Mühlenfeld – since September 20, 2007 -

Dr. Wolfgang Reiniger – until July 5, 2007 -

Dr. Manfred Schneider

Mediation Committee in accordance with Sec. 27, Par. 3 of the German Co-Determination Act (MitbestG)

Dr. Thomas R. Fischer (Chairman)

Frank Bsirske

Werner Bischoff

Dr. Manfred Schneider

Personnel Affairs Committee

Dr. Thomas R. Fischer (Chairman)

Frank Bsirske

Dr. Paul Achleitner

Heinz-Eberhard Holl

Günter Reppien

Uwe Tigges

Audit Committee

Carl-Ludwig von Boehm-Bezing (Chairman)

Werner Bischoff

Dr. Gerhard Langemeyer

Günter Reppien

Dr.-Ing. Ekkehard D. Schulz

Uwe Tigges

Nomination Committee

Dr. Thomas R. Fischer (Chairman)

Dr. Paul Achleitner

Heinz-Eberhard Holl

Executive Board

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- since October 1, 2007 -
CEO of RWE AG
- BATIG Gesellschaft für Beteiligungen mbH
- British American Tobacco (Industrie) GmbH
- British American Tobacco (Germany) Beteiligungen GmbH
- Deutsche Bahn AG
- SURTECO AG (Chairman)
- Volkswagen AG
- Hanover Acceptances Limited

Harry Roels*
- until September 30, 2007 -
Former CEO of RWE AG
- Deutsche Post AG
- RWE Dea AG (Chairman)
- RWE Energy AG (Chairman)
- RWE Power AG (Chairman)
- RWE Npower Holdings plc (Chairman)
- RWE Trading GmbH (Chairman)

Berthold Bonekamp
Executive Vice-President of RWE AG
- Berlinwasser Holding AG
- RWE Energy AG
- RWE Rhein-Ruhr AG (Chairman)
- RWE Westfalen-Weser-Ems AG (Chairman)
- Berliner Wasserbetriebe AöR
- RWE Npower Holdings plc
- VSE a. s.

Alwin Fitting
Executive Vice-President of RWE AG
- RWE Energy AG
- RWE Pensionsfonds AG
- RWE Systems AG (Chairman)
- European School of Management and Technology GmbH

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- since April 1, 2007 -
Executive Vice-President of RWE AG
- Deutsche Steinkohle Aktiengesellschaft
- RAG AG
- RheinEnergie AG
- RWE Dea AG
- RWE Energy AG (Chairman)
- RWE Power AG (Chairman)
- RWE Npower Holdings plc (Chairman)
- RWE Trading GmbH (Chairman)

Dr. Rolf Pohlig
Executive Vice-President of RWE AG
- RWE Energy AG
- RWE Pensionsfonds AG (Chairman)
- RWE Power AG
- American Water plc
- RWE Npower Holdings plc
- RWE Rhenas Versicherungsvermittlung GmbH (Chairman)

Dr. Klaus Sturany*
- until April 30, 2007 -
Former Executive Vice-President of RWE AG
- Bayer AG
- Commerzbank AG
- Hannover Rückversicherung AG
- Heidelberger Druckmaschinen AG
- Österreichische Industrieholding AG

Jan Zilius*
- until April 30, 2007 -
Former Executive Vice-President of RWE AG
- RAG AG
- RAG Beteiligungs-AG

- Member of other mandatory supervisory boards.
- Member of comparable domestic and foreign supervisory bodies of commercial enterprises.

* Information valid as of the date of retirement from the Supervisory Board.

Economic Advisory Board

Prof. Dr. Dr. Theodor Baums
Frankfurt am Main
Member of the Executive Committee of Deutsche Schutzvereinigung für Wertpapierbesitz e.V.

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- until October 31, 2007 -
Chairman of the Administrative Council of Adecco management & consulting S. A.

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Dr. Jürgen Großmann
- until September 30, 2007 -

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Essen
Former CEO of RWE AG

Prof. Dr. Hubert Markl
Constance
Former President of Max-Planck-Gesellschaft

Wolfgang Mayrhuber
Frankfurt am Main
CEO of Deutsche Lufthansa AG

Dr. Thomas Middelhoff
Essen
Chairman of the Management Board of Arcandor AG

Klaus-Peter Müller
Frankfurt am Main
Chairman of the Board of Managing Directors of Commerzbank AG

Dr. Udo Oels
Odenthal
- until September 30, 2007 -
Former Executive Vice-President of Bayer AG

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Munich

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Wolfsburg
- until September 30, 2007 -
Volkswagen AG

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Munich
Chairman of Schutzgemeinschaft der Kapitalanleger e.V.

Prof. Dr. Jürgen Strube
Ludwigshafen
Chairman of the Supervisory Board of BASF Aktiengesellschaft

Dr. Alfons Friedrich Titzrath
Cologne
- until May 15, 2007 -
Former Chairman of the Supervisory Board of Dresdner Bank AG

Anton Werhahn
Neuss
Business executive

Glossary

BAFA price. Germany's Federal Office of Economics and Export Control (BAFA) uses reports made by buyers of hard coal to determine the price paid in Germany, including all costs incurred from the German border to the buyer. The price of power plant hard coal is published by BAFA quarterly and annually in shipping tons and tons of hard coal units.

Barrel. International unit of measurement for trading petroleum, available in imperial and US variants. A US barrel corresponds to 158.987 litres.

Clean Development Mechanism. In accordance with the Kyoto Protocol, companies and countries can obtain emissions certificates by participating in projects to reduce emissions in newly developing and developing countries, which are not obliged to reduce emissions themselves. They can use these certificates to meet their own requirements.

Combined heat and power generation. Heat which is not used in conventional thermal power generation plants is captured and used as steam or hot water. This increases the fuel efficiency of a power plant.

Commercial paper. Tradable, unsecured bearer bond issued only for short-term debt financing. Commercial paper is a revolving credit facility, with terms typically ranging from one day to 24 months.

Commodity. Term for standardized, tradable goods such aswheat, oil or gas.

Confidence interval. Range of probability used when estimating a parameter. The confidence interval is expressed in degrees of probability.

Credit default swap (CDS). Financial derivative for trading default risks associated with debt financing. The party seeking to hedge such risks generally pays an annual fee to the principal. In the event that the underlying credit is not repaid, the hedge-seeking party receives a contractually agreed sum from the principal.

Debt issuance programm. Contractual master and model documents for the issuance of bonds on domestic and foreign markets. It can be used as a flexible financing vehicle to issue long-term debt.

Defined benefit obligation. Net present value of anemployee's benefit entitlements as of the balance-sheetdate.

EBITDA. Earnings before interest, taxes, depreciation andamortization.

Equity accounting. Method for accounting for entities whose assets and liabilities cannot be entirely included in the consolidated financial statements by fully consolidating the entity. In such cases, the carrying amount of the investment is recorded on the basis of the development of the share held in the entity's equity. This change is recorded in the income statement of the company which owns the share in the entity.

Forward market/forward trading. Contracts for transactions to be fulfilled at a fixed point in time in the future are traded on forward markets. The price of the forward is established when the contract is agreed.

Hard coal unit (HCU). Unit of measurement for the energy content of primary energy carriers. One kilogram HCU corresponds to 29,308 kilojoules.

Incentive-based regulation. Regulation model which will replace the current German cost control system from 2009 onwards. Based on the new model, grid fees will no longer be calculated on the basis of individual costs alone. Instead, the main parameter will be the cost base of the most efficient grid operators, based on a model established by the regulator.

Joint implementation. In accordance with the Kyoto Protocol, companies and countries can obtain emissions certificates by participating in projects to reduce emissions in certain other countries which are obliged to reduce emissions. They can use these certificates to meet their own reduction requirements.

LNG. Acronym for liquefied natural gas. LNG is obtained by cooling gas until it becomes liquid. It occupies only 1/600 of the space filled by natural gas in its gaseous state. Therefore, it is very well suited for transportation and storage.

Megawatt (MW). Unit of measurement of electric output. 1 megawatt = 10^3 kilowatts, 1 gigawatt = 10^6 kilowatts, 1 terawatt = 10^9 kilowatts.

Past service cost. Reflects the rise in the net present value of a defined benefit obligation attributable to an employee's service in past reporting periods.

Pensionsfonds. Separate legal entity under the supervision of the German Federal Financial Supervisory Authority. Legal standing differs from that of typical UK and US pension funds.

Performance shares. Virtual shares, which entitle plan participants to receive a payment at the end of the three-year plan period. Performance shares are not exercised individually. They are paid out in cash at the end of the period if the pre-defined performance targets have been met or exceeded.

Rating. Standardized method in international capital markets for assessing the risk exposure and creditworthiness of debt issuers. A Single A rating is given to borrowers of strong creditworthiness.

Service cost. Reflects the increase in the cost associated with the net present value of an employee's benefit entitlements in accordance with the employee's work performance in the period being reviewed.

Spot market/spot trading. General term for markets where payment and delivery are effected immediately on conclusion of the transaction.

Spread. Difference between the buying and selling price. As regards bonds, the spread represents the difference in yield on bonds from different issuers.

Syndicated credit line. Credit line offered to companies, backed by several banks, with a term of one to seven years. Can be drawn down in various amounts, terms and currencies. Generally used to secure liquidity.

Total Shareholder Return (TSR). Indicator of the development of a share investment over the long term. It takes into account both the dividends paid as well as the changes in share price for the duration of the investment.

Upstream. Term for all activities involved in the exploration and production of oil and gas. Also includes the processing of these resources into marketable raw materials meeting generally accepted quality standards.

Value-at-risk method. Measure of risk indicating the estimated maximum loss that might occur from a risk position, assuming a certain probability under normal market conditions and that the position is held for a certain period of time.

Index

Imprint

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Five-year overview RWE Group		2007	2006[1]	2005	2004	2003
External revenue	€ million	42,507	42,554	39,487	42,137	43,875
Income						
EBITDA	€ million	7,902	7,172	7,095	8,400	8,476
Operating result	€ million	6,520	5,681	5,371	5,976	5,551
Income from continuing operations before tax[2]	€ million	5,233	3,537	3,156	3,935	2,123
Net income/RWE AG shareholders' share in net income[2]	€ million	2,659	3,847	2,231	2,137	953
Earnings per share[2]	€	4.73	6.84	3.97	3.80	1.69
Return on equity	%	19.9	30.3	20.8	23.8	10.4
Return on revenue	%	16.0	15.2	13.6	15.1	10.2
Value management[3]						
Return on Capital Employed (ROCE)	%	16.4	14.2	16.6	13.5	10.4
Value added	€ million	2,957	2,074	2,451	1,998	781
Capital employed	€ million	39,710	40,206	32,444	44,480	53,961
Cash flow/capital expenditure/depreciation and amortization						
Cash flows from operating activities	€ million	6,085	6,783	5,304	4,928	5,289
Free cash flow[4]	€ million	2,020	2,289	1,637	1,499	927
Capital expenditure including acquisitions	€ million	4,227	4,728	4,143	3,737	9,762
Property, plant and equipment	€ million	4,065	4,494	3,667	3,429	4,362
Depreciation, amortization, impairment losses and asset disposals[5]	€ million	2,629	3,164	4,098	7,051	6,819
Free cash flow per share	€	3.59	4.07	2.91	2.67	1.65
Workforce						
Workforce at end of fiscal year[6]		63,439	61,725	85,928	97,777	127,028
Asset/capital structure[7]						
Non-current assets	€ million	41,580	51,999	71,680	65,406	66,731
Current assets	€ million	42,051	41,456	37,778	27,964	32,411
Balance sheet equity	€ million	14,918	14,111	12,357	11,193	9,065
Non-current liabilities	€ million	36,770	52,402	65,065	60,321	61,327
Current liabilities	€ million	31,943	26,942	32,036	21,856	28,750
Balance sheet total	€ million	83,631	93,455	109,458	93,370	99,142
Net financial debt of continuing operations	€ million	-2,064	-4,720	11,438	12,385	17,838
Net debt of the RWE Group[8]	€ million	5,056	6,864	23,435	24,238	30,141
Equity ratio	%	17.8	15.1	11.3	12.0	9.1

Five-year overview RWE Aktiengesellschaft		2007	2006	2005	2004	2003
Dividend/dividend payment						
Dividend payment	€ million	1,772[9]	1,968	984	844	703
Dividend per share	€	3.15[9]	3.50	1.75	1.50	1.25
Market capitalization/rating						
Market capitalization at the end of fiscal year	€ billion	53.5	46.5	34.9	22.6	17.5
Long-term credit rating						
Moody's		A1	A1	A1	A1	A1
(outlook)		(stable)	(stable)	(stable)	(negative)	(negative)
Standard & Poor's		A+	A+	A+	A+	A+
(outlook)		(negative)	(negative)	(negative)	(negative)	(negative)

1 Some figures adjusted; see commentray on page 60.
2 As a result of a change in IFRS, figures after 2003 do not include goodwill amortization.
3 Figures for 2006 and 2007 according to the new value management concept; see commentary on pages 72 et seq. and 208 et seq.
4 Cash flows from operating activities minus capital expenditure on property, plant and equipment.
5 In accordance with IAS 1, as of 2005 excluding financial assets.
6 Converted to full-time positions; the Water Division is not included in 2006 and 2007 figures.
7 Balance sheet structure in accordance with IAS 1 as of December 31, 2004;
2003: non-current assets = fixed assets including deferred taxes; current assets = inventories, accounts receivable and other assets, marketable securities, cash and cash equivalents and prepaid expenses.
8 Net financial debt plus provisions for pensions and similar obligations.
9 Proposed dividend for RWE AG's 2007 fiscal year, subject to approval by the April 17, 2008, Annual General Meeting.

Financial Calendar 2008/2009[1]

04/17/2008 Annual General Meeting

04/18/2008 Ex-dividend date

05/15/2008 Interim report for the first quarter of 2008 with analyst conference call

08/14/2008 Interim report for the first half of 2008
- Press conference
- Analyst conference

11/11/2008 Interim report for the first three quarters of 2008 with analyst conference call

02/26/2009 Annual report for fiscal 2008
- Press conference
- Analyst conference

04/22/2009 Annual General Meeting

04/23/2009 Ex-dividend date

05/14/2009 Interim report for the first quarter of 2009 with analyst conference call

08/13/2009 Interim report for the first half of 2009
- Press conference
- Analyst conference

11/12/2009 Interim report for the first three quarters of 2009 with analyst conference call

1 All events will be broadcast live on the Internet and can thus be followed by the public at large, investors and analysts simultaneously. We will keep the recordings on our website for at least twelve months.

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RWE | Annual Report 2007

RWE AG, ESSEN, GERMANY
CONSOLIDATED INCOME STATEMENT OF THE RWE GROUP [(1)]
FOR THE SIX MONTHS ENDED DECEMBER 31, 2007

Exchange rates			1,4721	1,3170 [(2)]
	Euros in millions (except for per share data) Three months ended Dec 31		**U.S. dollars in millions (except for per share data) Three months ended Dec 31**	
	2007	**2006**	**2007**	**2006**
Revenue (including natural gas tax / electricity tax)	**42.507**	**42.554**	**62.575**	**56.044**
Natural gas tax / electricity tax	-1.454	-1.385	-2.141	-1.824
Revenue	**41.053**	**41.169**	**60.434**	**54.220**
Changes in finished goods and work in progress / other own work capitalized	128	220	188	290
Cost of materials	-26.533	-27.123	-39.059	-35.721
Staff costs	-3.964	-4.620	-5.835	-6.085
Depreciation, amortization, and impairment losses	-2.257	-2.265	-3.323	-2.983
Other operating result	-2.653	-2.820	-3.905	-3.714
Income from operating activities of continuing operations	**5.774**	**4.561**	**8.500**	**6.007**
Income from investments accounted for using the equity method	447	409	658	539
Other income from investments	150	381	221	502
Financial income	3.206	2.982	4.719	3.927
Finance costs	-4.344	-4.796	-6.395	-6.317
Income from continuing operations before tax	**5.233**	**3.537**	**7.703**	**4.658**
Taxes on income	-2.076	-966	-3.056	-1.272
Income from continuing operations	**3.157**	**2.571**	**4.647**	**3.386**
Income from discontinued operations	-274	1.442	-403	1.899
Income	**2.883**	**4.013**	**4.244**	**5.285**
Minority interest	-224	-166	-330	-219
Net income / income attributable to RWE AG shareholders	**2.659**	**3.847**	**3.914**	**5.066**
	Euros	**Euros**	**U.S. dollars**	**U.S. dollars**
Basic and diluted earnings per common and preferred share	**4,73**	**6,84**	**6,96**	**9,01**
of which: from continuing operations	5,22	4,28	(7,68)	(5,64)
of which: from discontinued operations	-0,49	2,56	-(0,72)	(3,37)

(1) Prior-year figures restated.

(2) As required by the order all numbers were converted to U.S. dollars using the exchange rates existing at the end of the period.

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RWE AG, ESSEN, GERMANY
CONSOLIDATED BALANCE SHEET OF THE RWE GROUP
AS OF DECEMBER 31, 2007

Exchange rates			1,4721	1,3170 (1)

ASSETS	**Euros in millions**		**U.S. dollars in millions**	
	December 31 2007	**December 31 2006**	**December 31 2007**	**December 31 2006**
Non-current assets				
Intangible assets	11.882	14.901	17.492	19.625
Property, plant and equipment	20.038	26.034	29.498	34.287
Investment property	153	225	225	296
Investments accounted for using the equity method	2.421	2.271	3.564	2.991
Other non-current financial assets	1.011	1.684	1.488	2.218
Accounts receivable and other assets	3.619	3.266	5.328	4.301
Deferred taxes	2.456	3.618	3.615	4.765
	41.580	**51.999**	**61.210**	**68.483**
Current assets				
Inventories	2.352	2.226	3.462	2.932
Trade accounts receivable	8.816	8.876	12.978	11.690
Accounts receivable and other assets	9.493	10.772	13.975	14.187
Marketable securities	10.858	16.788	15.984	22.110
Cash and cash equivalents	1.922	2.794	2.829	3.679
Assets held for sale	8.610	0	12.675	0
	42.051	**41.456**	**61.903**	**54.598**
	83.631	**93.455**	**123.113**	**123.081**

EQUITY AND LIABILITIES	**Euros in millions**		**U.S. dollars in millions**	
	December 31 2007	**December 31 2006**	**December 31 2007**	**December 31 2006**
Equity				
RWE Group interest	14.131	13.439	20.802	17.699
Minority interest	787	672	1.159	885
	14.918	**14.111**	**21.961**	**18.584**
Non-current liabilities				
Provisions	21.212	28.632	31.226	37.708
Financial liabilities	10.046	15.672	14.789	20.640
Other liabilities	3.584	5.021	5.276	6.613
Deferred taxes	1.928	3.077	2.838	4.053
	36.770	**52.402**	**54.129**	**69.014**
Current liabilities				
Provisions	5.713	5.434	8.410	7.157
Financial liabilities	3.239	3.710	4.768	4.886
Trade accounts payable	8.054	8.148	11.856	10.731
Liabilities held for sale	5.875	0	8.649	0
Other liabilities	9.062	9.650	13.340	12.709
	31.943	**26.942**	**47.023**	**35.483**
	83.631	**93.455**	**123.113**	**123.081**

(1) As required by the order all numbers were converted to U.S. dollars using the exchange rates existing at the end of the period.

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RWE AG, ESSEN, GERMANY
CONSOLIDATED CASH FLOW STATEMENT OF THE RWE GROUP
FOR THE SIX MONTHS ENDED DECEMBER 31, 2007

	Euros in millions Three months ended Dec 31		U.S. dollars in millions Three months ended Dec 31	
Exchange rates			1,4721	1,3170 (1)
	2007	**2006**	**2007**	**2006**
Income	2.883	4.013	4.244	5.285
Depreciation, amortization, impairment losses, write-backs	2.512	3.025	3.698	3.984
Changes in provisions	438	1.300	645	1.712
Deferred taxes / non-cash income and expenses / income from disposal of non-current assets and marketable securities	474	-1.021	698	-1.345
Changes in working capital	-222	-534	-327	-703
Cash flows from operating activities	**6.085**	**6.783**	**8.958**	**8.933**
Capital expenditure on non-current assets	-4.220	-4.728	-6.212	-6.227
Proceeds from sale of assets	877	7.854	1.291	10.344
Changes in marketable securities and cash investments	-1.140	-5.597	-1.678	-7.371
Cash flows from investing activities	**-4.483**	**-2.471**	**-6.599**	**-3.254**
Cash flows from financing activities	**-2.458**	**-2.948**	**-3.618**	**-3.883**
Net cash change in cash and cash equivalents	-856	1.364	-1.260	1.796
Effects of changes in foreign exchange rates and other changes in value on cash and cash equivalents	-16	-1	-24	-1
Net change in cash and cash equivalents	**-872**	**1.363**	**-1.284**	**1.795**
Cash and cash equivalents at beginning of reporting period	2.794	1.431	4.113	1.885
Cash and cash equivalents at end of reporting period	**1.922**	**2.794**	**2.829**	**3.680**

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